

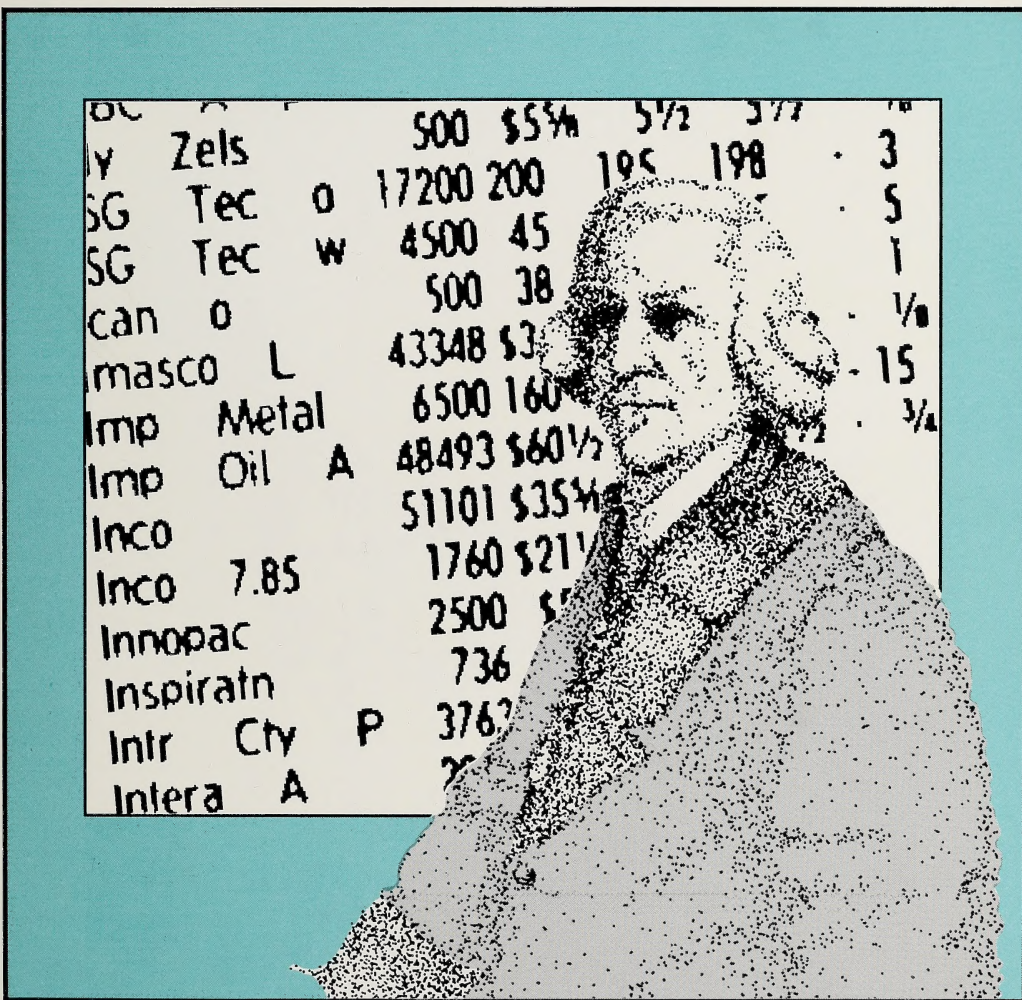
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# 3 CAPITALISM




S O C I A L S T U D I E S 3 0



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# **Social Studies 30**

## **Module 3**

# **CAPITALISM**



**Distance  
Learning**





This document is intended for	
Students	✓
Teachers (Social Studies 30)	✓
Administrators	
Parents	
General Public	
Other	

Social Studies 30  
 Student Module  
 Module 3  
 Capitalism  
 Alberta Distance Learning Centre  
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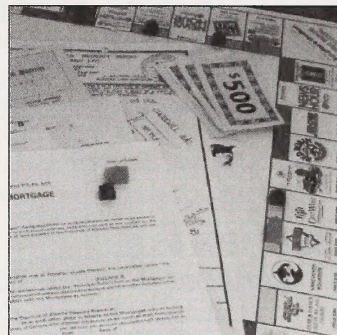
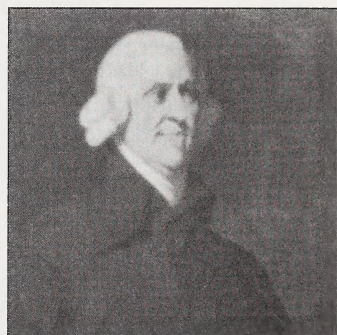


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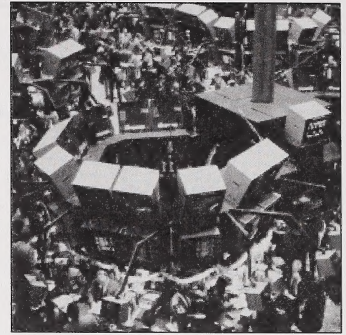
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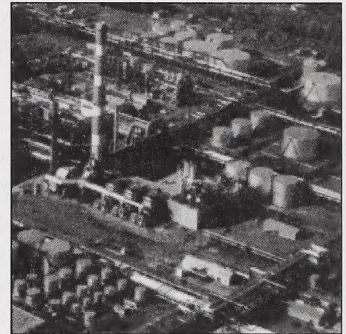
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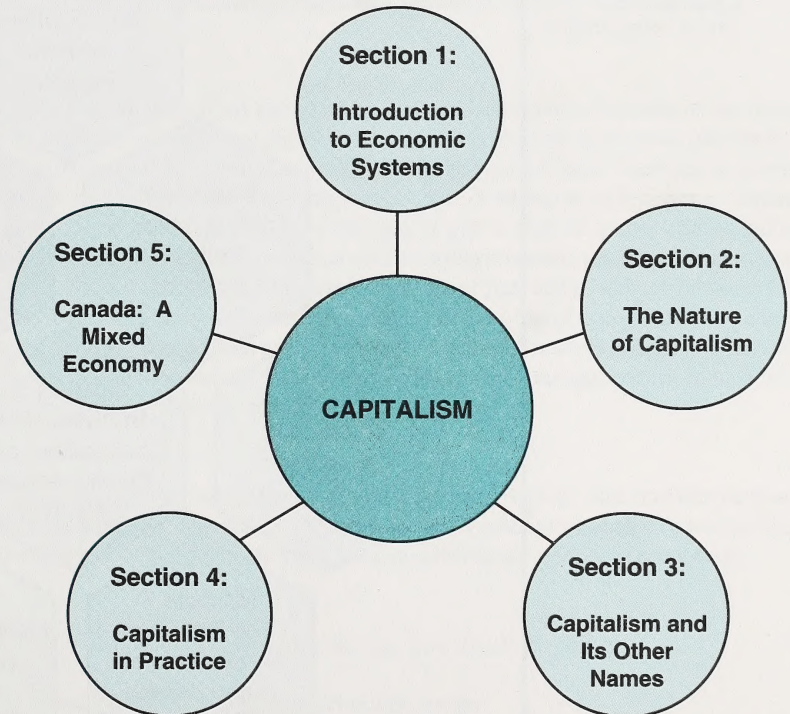
## OVERVIEW

Economics is a part of your life whether you like it or not. There is no way to escape it. In life and in the world at large you will need to know what is happening. If you do not learn the basic rules of economic systems, you put yourself at a disadvantage. For this reason it is essential that you have a good understanding of economic systems and their purpose. One way or another you will learn the rules of the game.

In this module you will examine the basic differences between capitalism and socialism. Then you will trace the development of capitalism, its theory, and its practical application. The final section of the module will examine the role of the Canadian government in the economy. As you make your way through this module, you will see how economic systems have adapted elements of both capitalism and socialism leaving the world with a series of mixed economies. However, the ideologies of capitalism and socialism serve as **benchmarks** by which you may compare the mixed economies of the world.

***Benchmark:** a point of reference for comparison*

This module is divided into five sections as follows:



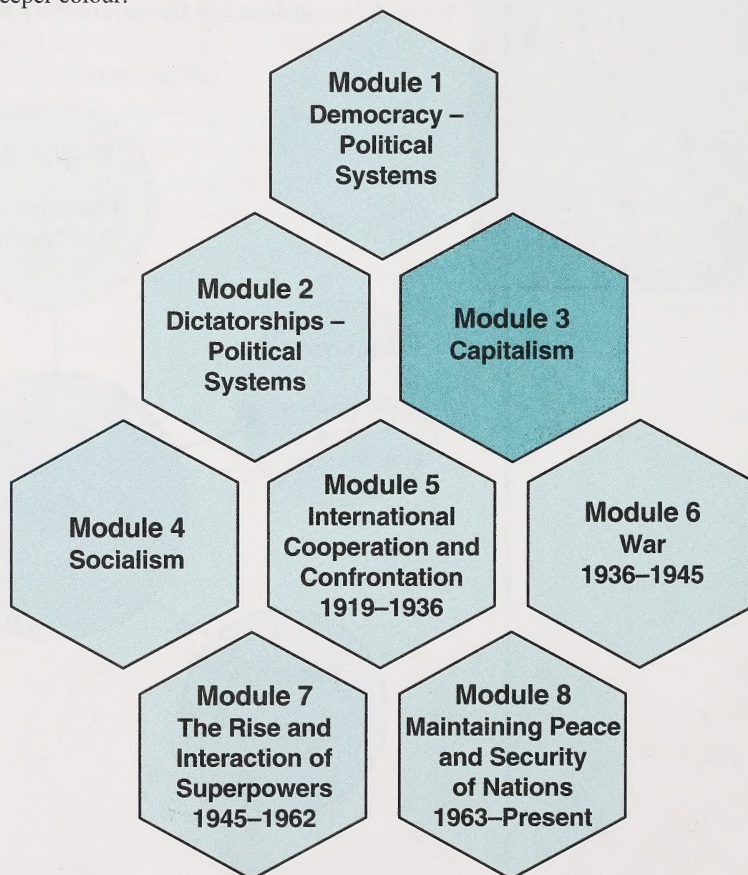
## Evaluation

Your mark in this module will be determined by your work in the Assignment Booklet. You must complete all assignments. In this module you are expected to complete two section assignments and one final module assignment. Your grade on this module will be calculated as follows:

Section 2 Assignment	25 marks
Section 4 Assignment	30 marks
Final Module Assignment	45 marks
<b>TOTAL</b>	<b>100 marks</b>

## Course Overview

This course contains eight modules. The module you are working on is highlighted in a deeper colour.





# Introduction to Economic Systems

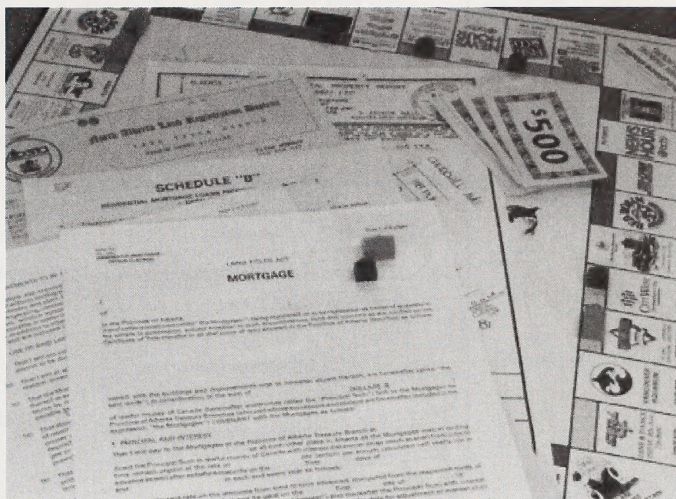


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**H**ave you ever played any games where you could buy and own property as you moved along the board, or played any games simulating life choices where you could play the stock market if you landed on certain squares? These are the types of games where someone needs to be the banker who gives the appropriate amount of money to each player as required. Game rules state how much money each player gets to start the game, when additional money is to be paid to a player, and what amounts a player needs to pay for landing on certain squares. What would happen if you tried to play one of these games without following these rules? Different games will have different rules but some sort of system has to be followed for the game to proceed in an orderly organized manner. Similarly in real life some set of rules or organized system which help determine how economic decisions will be made must exist for people in different countries.

**W**hat are economic systems, and why do they exist? Why do some countries have such different economic systems in comparison to the Canadian system? To answer these questions you will examine the basic principles behind the science of economics.

**W**hen you have completed this section, you should be able to

- understand the need for an economic system
- differentiate between capitalism and socialism
- understand important economic terms and concepts

## Activity 1: Capitalism Versus Socialism

There are two basic economic systems that place an emphasis in very different areas. Capitalism stresses an individualistic philosophy, as indicated in the following chart.



Socialism, the other basic economic system, promotes group welfare as shown in the following chart.



The economic systems of nations in today's world are not simply capitalist or socialist. Many nations have had to adapt their economic system as times changed and economics became more complex. Economic systems now have elements of both capitalism and socialism. They are mixed economies.

An economic system is based on a particular approach to economics. Capitalism, for example, is based on an approach to economics that promotes private enterprise. In a private enterprise system, you will see profit, initiative, competition, incentive, and self-advancement. Under a socialist system, you will see a more cooperative, equal, and collective system.

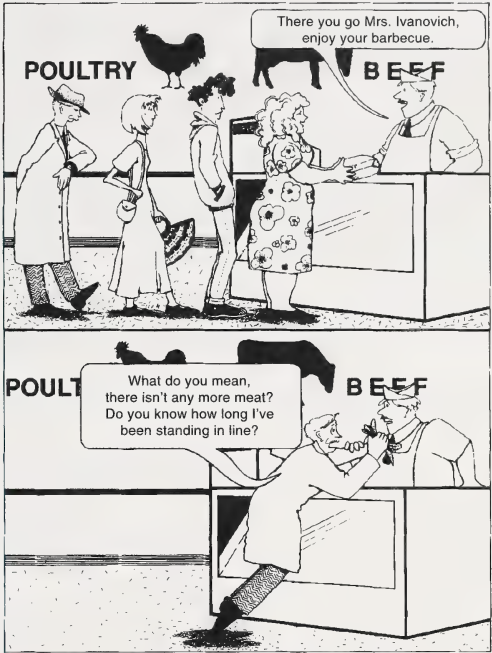
In order to understand these basic economic systems, it is necessary to have knowledge of economics. An economic system is a set of arrangements for dealing with scarcity. The problem of scarcity is the most important aspect of economics.

Economics can be defined as the science of scarcity. In many cases, one's **needs** and **wants** exceed the supply of goods. There are simply not enough resources for everybody to have everything they want. The problem then becomes satisfying needs and wants with limited resources. Resources are usually divided into three categories: land (natural resources and real estate), labour (the actions of people), and capital (human-made goods involved in the production of other goods). Every country must decide how to make the best use of its resources in order to solve the problem of scarcity.

*Needs: the desires for things which are essential for survival*

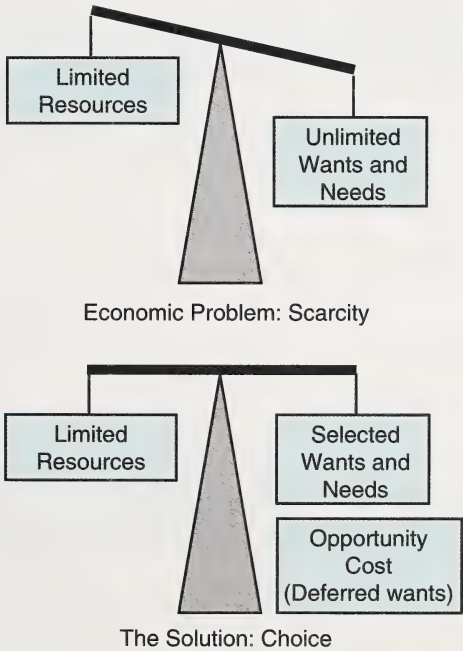
*Wants: the desires for things which are not essential*





*Scarcity: an economic condition (problem) caused by unlimited wants and needs in the light of limited resources*

Because of the economic problem of **scarcity**, people are forced to make choices.



*Opportunity cost: the cost of making an investment that is the difference between the return on one investment and the return on an alternative investment*

*The three economic questions: What to produce? How to produce it? Who gets what share of the production?*

Choice implies setting aside certain needs and wants. What will you buy now, and what can you wait to buy? What you decide not to buy because you buy something else is called the **opportunity cost**. For example, if you want to buy a new compact disc and a book, but you have only enough money for one item, you must make a choice. If you buy the compact disc, the book is the opportunity cost.

No matter what economic system evolves, all nations must first know the resources available, and then answer **three basic economic questions**:

- what to produce?
- how to produce it?
- who gets what share of that production?

The way in which these questions are answered varies from country to country.

1. List the three types of resources.

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2. Define scarcity.

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3. What are the three basic economic questions that must be answered by all societies?

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4. Why do all societies face the problem of scarcity?

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Check your answers by turning to the Appendix, Section 1: Activity 1.



Some economic systems stress individualism. The economic questions that concern society are answered by individuals. Individual initiative, individual decision making, self-interest, and competition are all stressed and are the basis for answering the three economic questions.

Other economic systems promote collectivism. The economic questions are answered based on what is in the best interest of the group. Collectivists emphasize group welfare, cooperation, centralized economic planning, and equality. A central body answers the three basic economic questions.

From these two different sets of attitudes and beliefs come two different economic systems: capitalism and socialism.

5. Explain the basic differences between capitalism and socialism.

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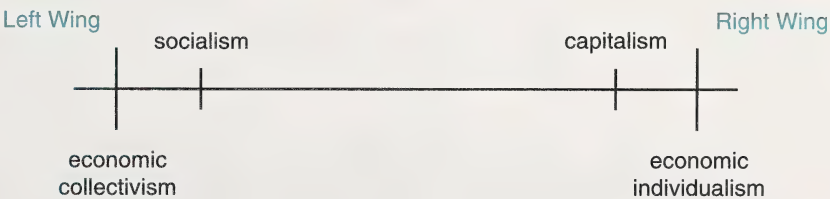
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Check your answers by turning to the Appendix, Section 1: Activity 1.

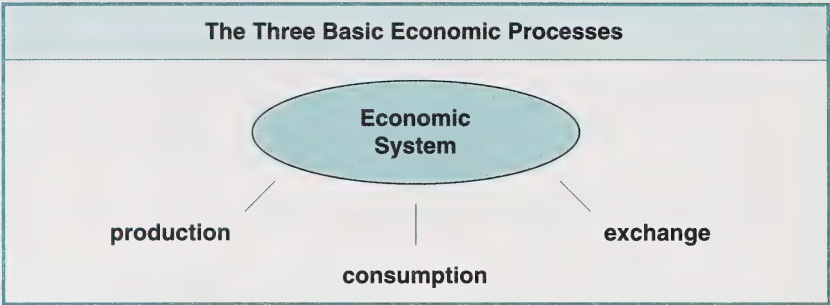
It is important to realize that there are no pure examples of either system in existence today. Nations today use parts of each system. These systems are referred to as mixed economies.

The two economic systems can be placed on a continuum such as this:



## Activity 2: Three Basic Economic Processes

Economics starts with human wants and ends with their satisfaction. In dealing with scarcity, an economic system is involved in three basic processes. These processes are production, exchange, and consumption.



*Goods:* items that are used in production or sold to consumers

*Services:* activities performed to earn wages

Before anything can occur in an economic system, something must be produced or performed. Those things produced or performed are called goods and services. **Goods** are either those items used in production or those items sold to consumers. **Services** are activities performed to earn wages.

1. The following list identifies some goods and services. Add five examples of your own.

Goods	Services
refrigerator guitar hot dog car bike stereo	haircut insurance sales firefighting teaching legal services



Once something has been made, the producer will likely want to sell it to a buyer or a consumer. This will involve an exchange. Exchange deals with the buying, selling, and pricing of goods. In order for exchange to take place, a market must be established. A market is a set of arrangements for bringing buyers and sellers together. Once a market has been established, some method of exchange is needed. The point at which exchange will occur is the market price (equilibrium point). This point is where the quantity of goods for sale at a certain price is equal to the quantity of goods the buyer is willing to buy.

When consumers are ready to buy, they must have some means to purchase the goods. In other words they must have money.

Money can take many forms. Exchange for goods and services can be made using a cheque, cash, or perhaps even a credit card.



"Do you take American Express?"

1

*Money: an agreed-upon medium of exchange in the market*

**Money** is the medium of exchange in most economic systems of the world today.

Once goods have been produced, income has been earned, and goods and services have been exchanged for money, then the goods are consumed by the buyers (consumers).

**Production of goods and services**

→ \$Money\$ →

**Consumption of goods and services**

<sup>1</sup> Canadian Speakers' & Writers' Service Ltd. for the cartoon by Ben Wicks. Reprinted by permission of Canadian Speakers' & Writers' Service Ltd.

2. What is a market?

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3. Explain the following basic economic processes:

a. production

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b. exchange

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c. consumption

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4. How does exchange occur in the market?

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Check your answers by turning to the Appendix, Section 1: Activity 2.



## Follow-up Activities

If you had difficulties understanding the concepts in the activities, it is recommended that you do the Extra Help. If you have a clear understanding of the concepts, it is recommended that you do the Enrichment.

### Extra Help

Economics is the science of scarcity. Scarcity results when there are not enough resources (land, labour, and capital) for everyone to have everything they want or need.

Every country decides how to manage its resources to overcome the problem of scarcity. You have learned about two basic economic systems that deal with scarcity – capitalism and socialism – and you have learned about the differences in their philosophies.

Capitalists favour an environment in which individual initiative and the desire for profit deals with the problem of scarcity. Socialists try to deal with scarcity through collective action and centralized economic planning. In reality, there are no economic systems that are purely capitalistic or socialistic. They have elements of both.

There are three basic processes that take place in an economic system: production, exchange, and consumption. When a product or service is made available, the buyer (consumer) and seller come together. When they agree on a price (market price or equilibrium point), an exchange takes place.

More will be said about this topic in Section 3.

1. Match the following terms to the appropriate description.

- |                  |                          |               |
|------------------|--------------------------|---------------|
| a. mixed economy | c. economics             | e. scarcity   |
| b. socialism     | d. three basic resources | f. capitalism |

\_\_\_\_\_ an economic system associated with profit, competition, and incentive

\_\_\_\_\_ the basic economic problem

\_\_\_\_\_ land, labour, and capital

\_\_\_\_\_ science that attempts to solve the problem of scarcity

\_\_\_\_\_ an economic system that uses parts of both capitalism and socialism

\_\_\_\_\_ an economic system associated with cooperation, equality, and group welfare

2. Read the following statements and indicate, in the space provided, whether each one is true (T) or false (F).
- \_\_\_\_\_ a. Economics is the science of scarcity.
  - \_\_\_\_\_ b. Economic systems are organized to deal with scarcity.
  - \_\_\_\_\_ c. All nations are either capitalistic or socialistic.
  - \_\_\_\_\_ d. In most systems, limited wants are balanced by limited resources.
  - \_\_\_\_\_ e. Private business is more important in countries that are more capitalistic.
  - \_\_\_\_\_ f. Capitalism and collectivism mean about the same thing.
  - \_\_\_\_\_ g. In economic terms a bicycle is a type of service.
  - \_\_\_\_\_ h. The process of exchange goes together with markets.
  - \_\_\_\_\_ i. Money is the most common medium of exchange.
  - \_\_\_\_\_ j. The people who provide goods are consumers.

Check your answers by turning to the Appendix, Section 1: Extra Help.

Enrichment

Capitalism and socialism, the two economic systems mentioned in this section, are based on different attitudes and beliefs. The following chart is a summary.

Capitalism	Socialism
profit competition self-advancement incentive	equality cooperation nationalization group welfare

Look through a newspaper and attempt to locate news items or articles about countries with basically socialist and capitalist economies. Review the information in terms of the following chart.



Capitalism	Socialism
Name of Article: _____	Name of Article: _____
Place a check if you found evidence of	Place a check if you found evidence of
<input type="checkbox"/> profit <input type="checkbox"/> competition <input type="checkbox"/> self-advancement <input type="checkbox"/> incentive	<input type="checkbox"/> equality <input type="checkbox"/> cooperation <input type="checkbox"/> nationalization <input type="checkbox"/> group welfare

Write a composition of several paragraphs, describing the details that identify those elements of each system that you have found. Use your own paper.

## Conclusion

Economic systems are organized to deal with the production and distribution of goods and services in society.

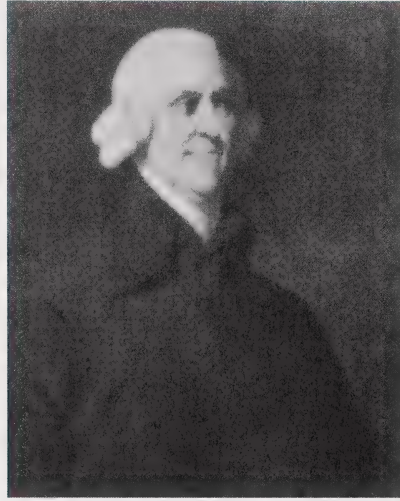
Capitalism and socialism are two economic systems that attempt to answer the same questions. However, the methods they use to answer these questions are completely different. One economic system (capitalism) stresses individualism while the other system (socialism) stresses collectivism or group welfare.

Capitalism will be explored in the remainder of this module while socialism will be more fully explored in Module 4.

## ASSIGNMENT

There is no assignment for this section.

# The Nature of Capitalism



Adam Smith

**T**he exchange of money for goods and services is part of the Canadian economic system. Have you ever thought about who thought up the basic principles of the economic system that form the major part of the Canadian economy? Adam Smith's beliefs formed the basis for the development of capitalism and the basic ideas for the free market.

**W**hat is capitalism? What caused people to develop an economic ideology that theoretically at least, gave them greater freedom? It is important to understand capitalism because of its role in the Canadian economy. This means that the knowledge which you will gain in this section will help you to better understand your own economic system.

**A**t the end of this section you should be able to do the following:

- understand the background role of mercantilism in the development of capitalism
- describe how Adam Smith's ideas were a reaction to mercantilism
- relate the impact of social Darwinism on the development of capitalism
- describe how the philosophy of individualism has effected the development of capitalism



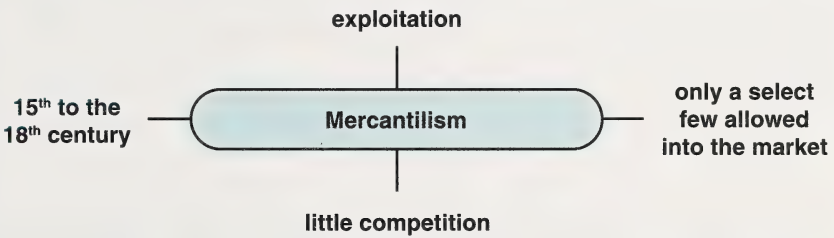
**Capitalism:** an economic system characterized by private or corporate ownership of capital goods

**Capital goods:** machinery, factories, tools, and anything else used in the production of goods

Activity 1: Mercantilism: A Background to Capitalism

Capitalism is an economic system which is based upon certain beliefs about human nature. **Capitalism** reflects the view that people desire to operate relatively free from economic restrictions and control. This means that people should be able to work where they want, start a business, and make a profit. Generally a capitalist wants to be as free as possible from government interference. For most of history, this was not the case. Capitalism takes its name from those who most strongly hold this view – the owners of **capital goods**.

Before the development of capitalism, there was an economic system called mercantilism. This system was in effect from approximately the fifteenth century to the eighteenth century. During this time, many of the heads of state in Europe were monarchs. Their sole aim was to make the nation as wealthy as possible, even if it meant exploiting other smaller nations. The monarch would grant certain merchants, friends, relatives, or companies a licence to operate their business enterprises. Granting privileges to operate businesses created monopolies with unfair economic advantages. Competition was almost non-existent. The monarch raised money by selling licences and taxing the merchants and companies that were making large profits through mercantilism.



1. What were the major advantages and disadvantages of mercantilism?

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2. How did mercantilism promote monopolies?

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3. How was the freedom of many people affected by monopolies?

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Check your answers by turning to the Appendix, Section 2: Activity 1.

Activity 2: Adam Smith and the Market Economy

*Market:* a set of arrangements for bringing buyers and sellers together

*Intervention:* government involvement in the economy with the intent to change, modify, or direct

You might say that the government was too involved in the **market** under mercantilism. There was too much **intervention**, according to one man named Adam Smith. Smith was a Scottish economist and philosopher who lived from 1723 to 1790. He wrote a book, *The Wealth of Nations*, which was a reaction to the excessive government control of the economy.

Smith believed that there had to be an economic system which better reflected his view of man’s competitive nature. His beliefs formed the basis for the development of capitalism.

The driving force of capitalism is the free market. This will be explained in more detail in Section 3. For now, you will examine some of the basic ideas underlying the free market of Adam Smith.

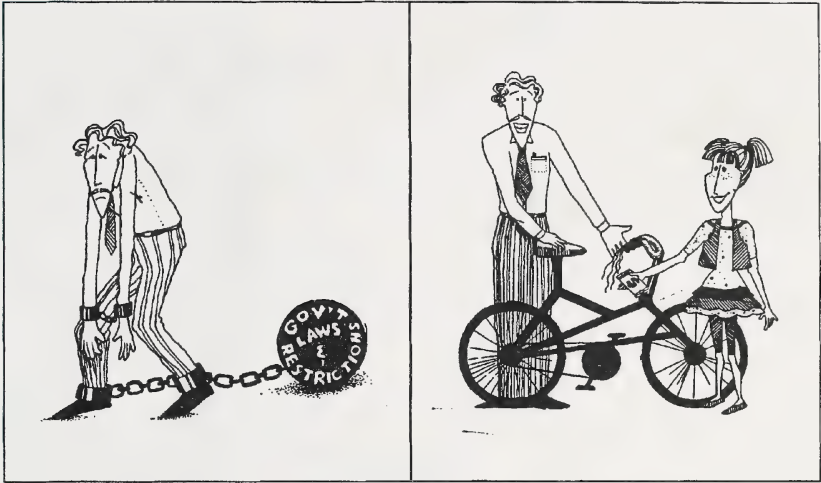
He felt that by having government intervene in the market or economy, economic growth was slowed. Smith believed that if you allowed individuals to pursue their own self-interest, all of society would benefit.

If producers act in their own self-interest, then their ultimate goal is to make as much money as possible. To do this the producers must sell their produce or service to buyers. The buyers, on the other hand, only have so much money and will only buy things they want or need. The sellers must find out what the buyers want to buy and produce these goods or services for them. The buyers and sellers then decide on a fair price. The buyers then have goods and services they want, and the sellers have their profits.



Economic Constraint

Economic Freedom



1. What is the role of self-interest in a market economy? Explain.

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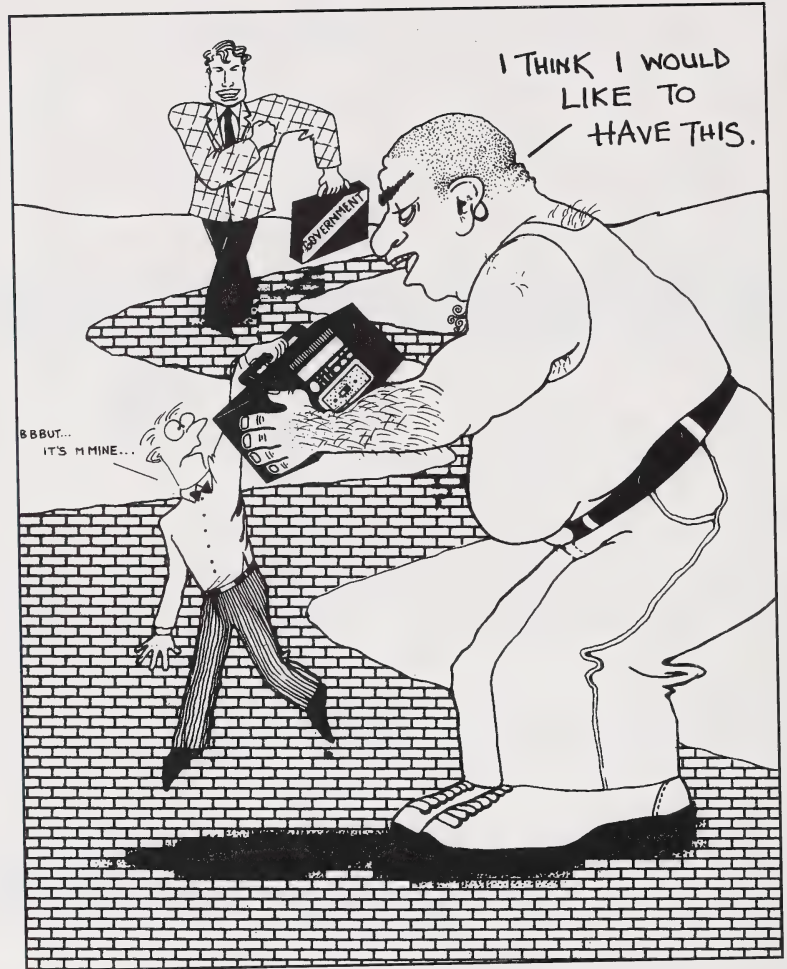
Check your answers by turning to the Appendix, Section 2: Activity 2.

*Economic competition: a system involving a large number of producers and sellers interacting in a free market*

*Private property: a good or service belonging to an individual or company*

*Contract: an arrangement to protect interests in an exchange of goods and services*

The only role that Smith saw for the government in the marketplace was to ensure a peaceful environment where perfect **economic competition** could exist. To achieve this peaceful economic environment, government had to guarantee the right of individuals to own **private property**. Also, the government was responsible for guaranteeing **contracts**. Imagine an economic system where there were no rules, a system where no one could rightly say, “I own this, and it is mine to do with as I like.” If one cannot be sure of ownership, there cannot be buying or selling. There would be nothing to stop the strongest, meanest person in a town from simply stating, “I want this, so I am going to take it.” There must be some sort of assurance in the market that this will not occur. This, according to Smith, was the government’s job.



The mercantile system was completely different from the capitalist system of Adam Smith. The following summary shows the differences between the two economic systems.

### Mercantilism

- The goal was for the nation and king or queen to acquire as much wealth as possible.
- There was very little competition.
- Nations exploited other countries.
- Monarch (ruler) decided who would be sold a licence to operate a business.

Generalization: Mercantilism extends the power of the government to intervene in the economy.



**Capitalism**

- open competition
- guaranteed private property
- economic freedom
- self-interest = profit

Generalization: Capitalism limits the power of the government to intervene in the economy.

2. Is the right to own private property necessary so that a person can earn a profit? Explain.

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3. Explain how economic freedom is related to competition.

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*Entrepreneur:* a person who manages and assumes the risks of business

4. Under which economic system would you prefer to be a merchant (**entrepreneur**): mercantilism or capitalism? Explain.

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Check your answers by turning to the Appendix, Section 2: Activity 2.

### Activity 3: Social Darwinism

A further theory which helped in the development of capitalism was social Darwinism. This theory was put forward by a man named Herbert Spencer. Spencer viewed society and one's position in society as being the result of evolutionary progression, or in simple terms, "the survival of the fittest." The market in which buyers and sellers are competing is like a battlefield where only a few will be left standing at the end.





The idea of social Darwinism, when examined in an economic situation, becomes economic Darwinism. Success or failure is measured in terms of profit. Those who fail go out of business.

Compose a sketch portraying the idea of “survival of the fittest” if it were to be used in an economic system. Remember, you are examining the nature of capitalism. Space is provided for you on this page to compose your sketch.

Review the sketch on the previous page and compare it with your sketch.

Check your answers by turning to the Appendix, Section 2: Activity 3.

### Activity 4: The Impact of Individualism

You are an individual. All individuals have different needs and wants. As you have seen so far in this section, capitalism tries to satisfy some of these needs. Mercantilism also attempted to satisfy the needs and wants of society, but it tried to do so differently than capitalism. The reason for this is that both of these economic systems viewed humanity differently. In fact, all economic systems have varied ideologies, or beliefs, that cause them to be different.

An important value of capitalism is individualism. Mercantilism placed restrictions on the freedom of the individual. There was a need for an economic system which recognized that all people were individuals. Under capitalism people were allowed to enter freely into the market.

Capitalism developed historically as a part of the movement of individualism. In religion, that movement produced the Reformation; in learning, the growth of the physical sciences; in human relations, the social sciences; in politics, democratic government; and in economics, the capitalist system.

The beliefs of capitalism gave the individual person the freedom to either succeed or fail, something which had been lacking under mercantilism.

Do you think capitalism is an economic system which reflects (shows) the true nature of human beings? Explain. If possible discuss this question with a partner.

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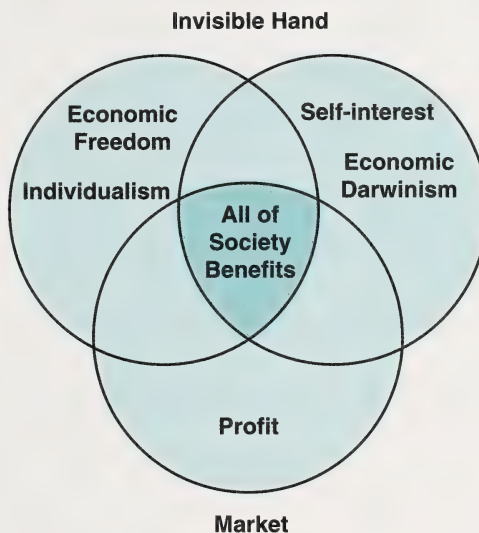
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Check your answers by turning to the Appendix, Section 2: Activity 4.

## Activity 5: The Invisible Hand

**Invisible hand:** the economic theory that states that all of society benefits indirectly through the actions of individuals or companies seeking profit

The **invisible hand**, as shown in the following graphic representation, is a concept within capitalism which ensures that the needs of society will be met.



Because of the search for profit, a producer will produce what society wants produced. This may seem unlikely. In terms of logic, if someone is looking after their own interests you would not expect them to serve your needs. However, there is a theory in economics which suggests that economic freedom can be associated with public welfare. This is simply because there is a financial benefit to businesses that provide what the people want as consumers. This was recognized as early as 1776 by Adam Smith in his book on economics, *The Wealth of Nations*. He pointed out that prices and the profit motive cause businesses to meet public needs even though their interest is in only their own profit. This is his still-famous quote on the subject:

[The business person] is led by an invisible hand to promote an end which was no part of his intention. Nor is it always the worse for the society that it was no part of it. By pursuing his own interest he frequently promotes that of society more effectually than when he really intends to promote it. I have never known much good done by those who affect to trade for the public good. It is an affectation, indeed, not very common among merchants, and very few words need be employed in dissuading them from it.

—Adam Smith



1. What is the invisible hand?

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2. Explain in a short paragraph how the invisible hand is supposed to work.

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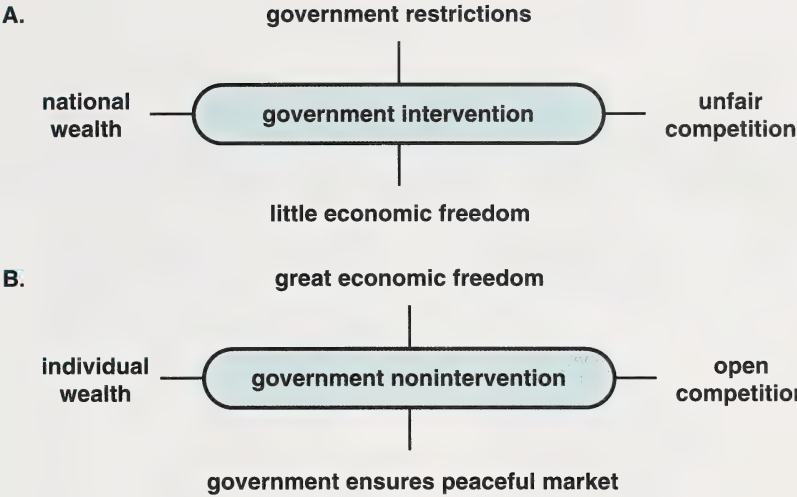
Check your answers by turning to the Appendix, Section 2: Activity 5.

## Follow-up Activities

If you had difficulties understanding the concepts in the activities, it is recommended that you do the Extra Help. If you have a clear understanding of the concepts, it is recommended that you do the Enrichment.

### Extra Help

Examine the following concept maps, and then answer the two questions. One concept map shows characteristics of mercantilism, the other shows characteristics of capitalism. Remember that intervention deals with the amount of government control in the economy.



1. Would the economic system of mercantilism be more correctly shown by concept map A or B? Explain.

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2. Would the economic system of capitalism be most correctly shown by concept map A or B? Explain.

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Check your answers by turning to the Appendix, Section 2: Extra Help.

## Enrichment

In the following enrichment activity you have a choice of **either** doing question 1, 2, **or** 3.

1. What is the government's role in a capitalist economic system? What importance is placed on the individual in capitalism?

[illegible]



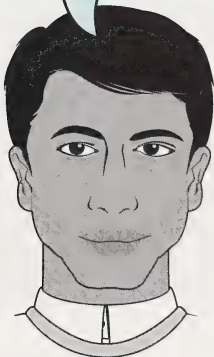
2. Read the following; then complete the discussion by filling in the empty speech balloons.

People are by nature concerned with their own self-interests!

But what about the people who can't look after themselves?

Too bad! Government must allow freedom in the market. Individuals must either succeed or fail.

Hold on! There must be a role for government!

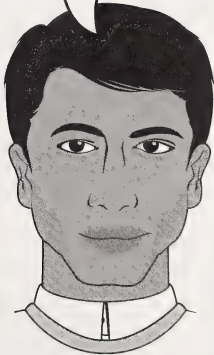


Empty speech balloon for the woman's response.

Empty speech balloon for the man's response.

Empty speech balloon for the woman's response.

Empty speech balloon for the man's response.





3. If you have the appropriate video equipment, view the videotape “*What is Capitalism?*” and complete the questions that follow. The video is an excellent introduction to capitalism. You should be looking for clarification of the nature of capitalism. Also, be aware of other terms used to describe capitalism: *market system*, *free enterprise system*, *laissez-faire*.

- a. Why do you think there are so many different terms to describe capitalism?

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- b. How does the term *laissez-faire* relate to capitalism?

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Check your answers by turning to the Appendix, Section 2: Enrichment.

## Conclusion

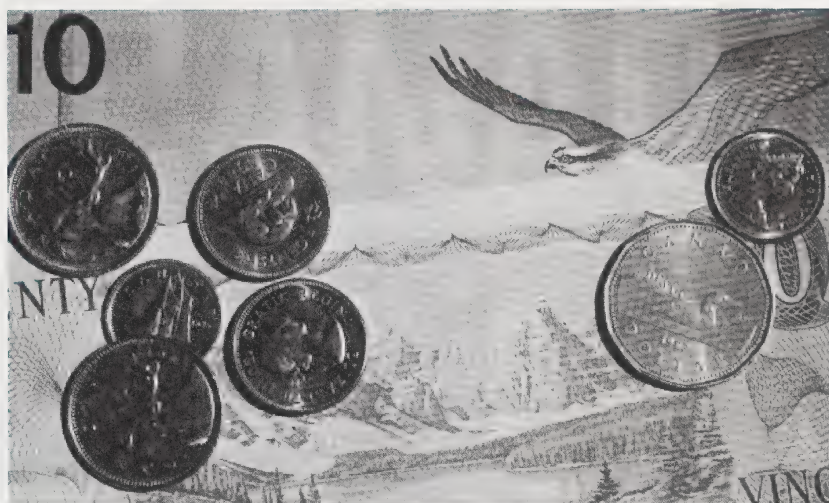
In this section you have examined some of the basic values and concepts of capitalism. It is an economic system that allows an individual the freedom to compete. Under capitalism there is theoretically equal opportunity for all to either succeed or fail in the search of profit. Government's role under capitalism is limited to ensuring a peaceful economic marketplace.

Assignment  
Booklet

## ASSIGNMENT

Turn to your Assignment Booklet and do the assignment for this section.

# Capitalism and Its Other Names



Other names for capitalism



What terms or words can you think of that relate to a Canadian one dollar coin? Perhaps you have used *loonie*, *dollar*, *one buck*, or some other term to refer to one dollar. Have you ever heard your grandparents or some older people refer to a quarter as “two-bits”? Different expressions or terms can be used for the same thing. Even when you think of people, you may have nicknames for certain friends or people that you know. In this section you will learn about some of the other terms or expressions that can be used to describe capitalism.

There are numerous synonyms for capitalism. This is because some parts of capitalism are so important that sometimes people name the economic system after a component of capitalism. For example, the role of the private citizen and private property in capitalism has led to the term *private enterprise*. In this section you will examine some of the key components of capitalism.

In this section you will

- identify the market in an economic system
- identify the role of specialization in capitalism
- define competition, private enterprise, and incentive
- understand the role of supply and demand in a capitalist economic system
- describe the relationship between private enterprise and capitalism

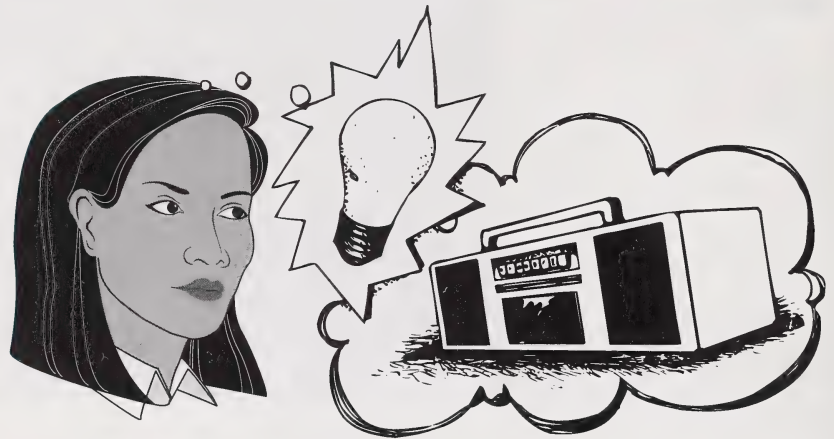


*Private enterprise: an economic system based upon the values of private business and individual freedom*

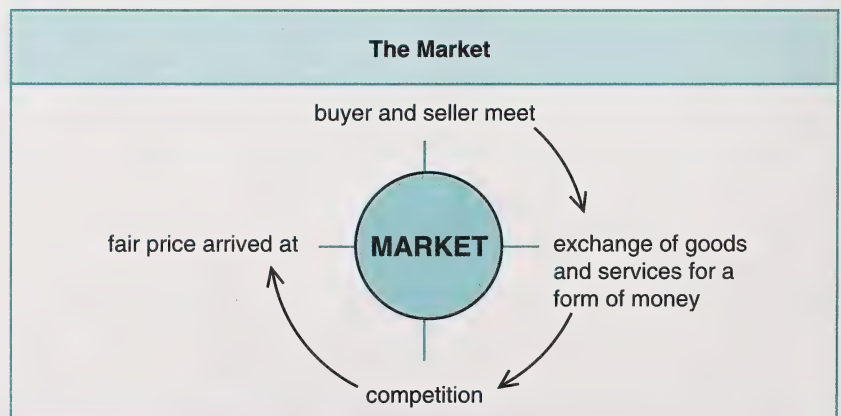
## Activity 1: The Role of the Market

Capitalism places a high value on **private enterprise**. The principle of private ownership of the means of production is the main feature of private enterprise.

Throughout this section you will learn how the private citizen can influence and direct an economic system because of individual freedom.



Capitalism is sometimes called private enterprise or the market system. The reason it is also called the market system is due to the importance of the market in a capitalist economic system. Remember, a market is a set of arrangements whereby buyers and sellers meet to exchange goods and services, often for some form of money. When you think of a market, what do you see? A bustle of activity? Merchants and producers selling their products? Buyers moving from seller to seller trying to get the best deal and the best product? The characteristics of a market have in many ways remained the same throughout history.



Imagine yourself in a present-day marketplace. You wish to buy a stereo. What do you do? You might begin by going down to a nearby shopping mall. In that shopping mall, you find that there are three stereo stores. Will you go to the first stereo store, buy a stereo, and leave? Or will you go to each of the stores and compare the products which you are interested in along with their prices? Most people will take the time to make an informed purchase, so that they know they are getting the best possible product for the price. You may also try to get the stereo you choose for less than the price tag reads because you want to save money. The sales clerk may accept your offer in order to get the commission. The market still exists in today's society, but it's just a little harder to see.

A Modern Market



Explain the purpose and function of a market in a private enterprise system.

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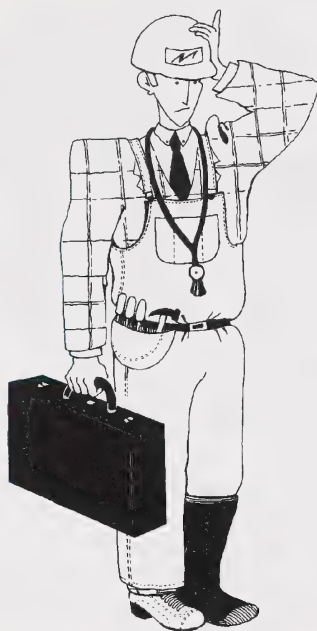
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Check your answers by turning to the Appendix, Section 3: Activity 1.

## Activity 2: Specialization

How would you like to make your own stereo? Would you even know where to begin? The market allows you to buy a stereo rather than having to make one. It allows people to become specialized in whatever job they choose. People are paid for the jobs they do with an accepted form of money; the money is then used to buy what the people want or need. Imagine a society where there was no market and you had to make whatever you wanted.

**Jack of All Trades**



**Specialization**



The more value that society places on a job, the greater is the reward for performing that job. Doctors are highly valued in our society, so they are rewarded with a larger income partly because there is a great demand for them. This income can then be used in the marketplace in exchange for other goods and services. Society places less demand on the job of bus driver; therefore, the bus driver has less money to exchange for goods and services.

*Productivity: the amount of goods or services produced in relation to the cost of production*

Because of specialization, a division of labour will also allow for greater **productivity** in an economy. If you are allowed to learn and do one job, you will become more productive. Division of labour, as seen by Adam Smith, allowed for more individualism – more happy people.



1. Define the word *specialization*.

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2. How does specialization increase production in the economy?

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3. Why is a doctor able to earn more money than a bus driver?

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Check your answers by turning to the Appendix, Section 3: Activity 2.

Activity 3: Private Enterprise Beliefs

It is important that you review three terms and their meanings at this time. They are **economic competition**, **individual incentive**, and **private property**.

Without private property guaranteed by law, the stereo shop owner would not be able to sell you a stereo. You simply must have private property in a private enterprise system (market system) if an exchange of goods and services is to occur. If you don't own it, you can't sell it. This is why the market system is also commonly known as private enterprise. The private enterprise system is an economic system based upon private ownership of the means of production: natural resources, factories, and equipment.

*Economic competition: a large number of producers and buyers interacting in a free market in search of profit*

*Individual incentive: the motivation for individuals to act in their own self-interest in the market*

*Private property: a good or service belonging to an individual or company*

Self-interest, or the profit motive, directs the actions of the stereo shop owner, and the best thing that can happen to him is to see a large profit.

The stereo shop owner's incentive is to produce a stereo that will sell. To do this the owner must convince you, the buyer, to buy the stereo. You, having your own self-interest, will only buy the stereo if you want or need it and it is of good quality at a fair price.

To ensure that quality and fair prices occur, there must be competition in the market. Because you, the buyer, have your own self-interest in mind, you will search out the best quality product at the best price.

Because there is more than one seller of stereos, they all must compete to produce a product better than their competitors and at a better price. This, of course, does not take into consideration two things that alter the situation: monopolies and advertising. These will be discussed in more depth in a later section.

1. Define competition.

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2. Define private property.

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3. Define individual incentive.

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Check your answers by turning to the Appendix, Section 3: Activity 3.

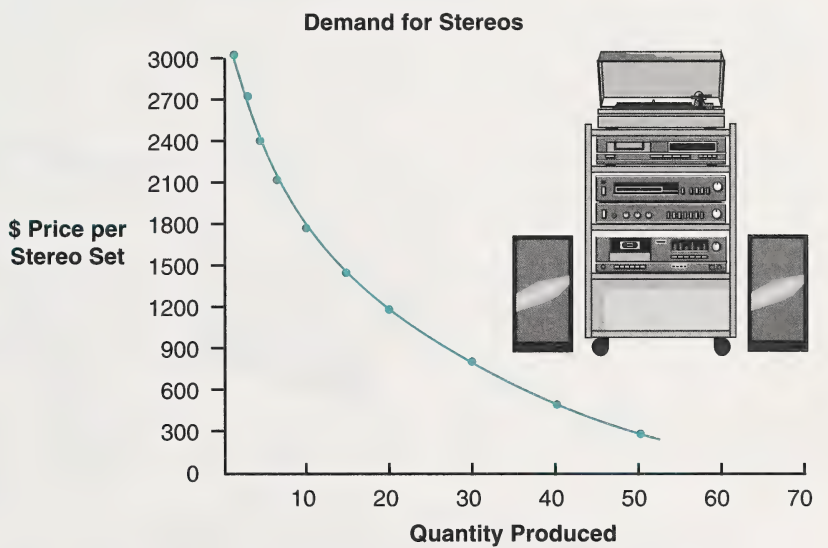
## Activity 4: Supply and Demand

Supply and demand act as an internal control on the production and distribution of goods in a society. The effects of supply and demand work to answer all of the basic economic questions. You will look at each (supply and demand) individually at first, and then examine them together to see the results.

**Demand**

Demand is most easily understood as being similar to desire. If you are willing to purchase a good or service that you desire, you are creating demand for it. When you go to the stereo shop and buy a stereo, you are giving the owner the incentive to stock more stereos.

If you decide that stereos are too expensive and you do not buy one, fewer stereos will be produced. So if you do not spend your money, fewer stereos will be made available for sale. So by either spending or holding on to your money, you have a small part in determining the supply of goods. Here is an example of a demand curve.



1. What is the price of stereos when the quantity produced is ten? Explain why so few are being sold.

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2. At what price is the demand for stereos the highest? Explain.

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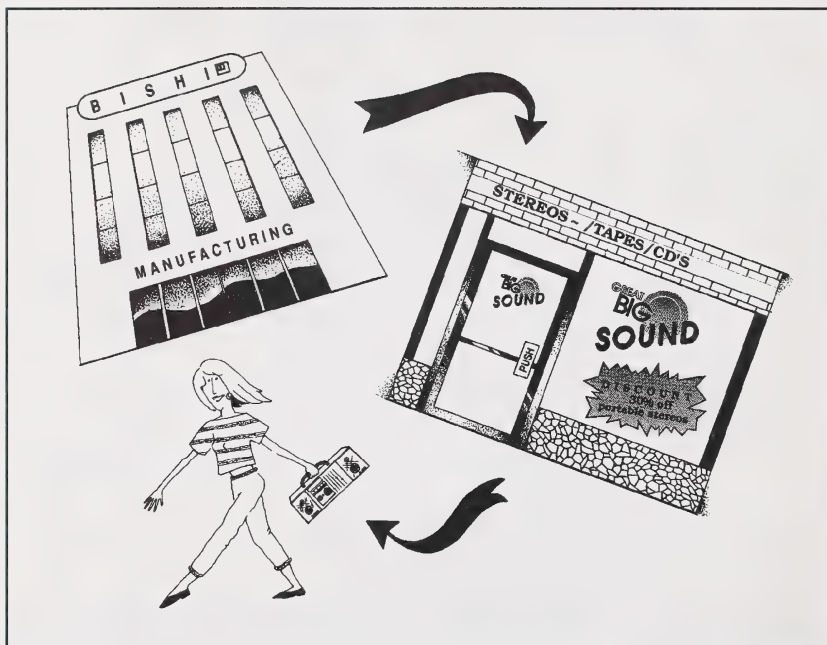


3. Write a “law of demand.” This should be a generalization which shows the general rule about demand; it has been started for you.

Law of Demand: When the price of a product goes up, \_\_\_\_\_ stereos\* will be sold. When the price of a product goes down, \_\_\_\_\_ stereos will be produced.

\* Stereos are just being used as an example. Any product or service could be substituted.

Check your answers by turning to the Appendix, Section 3: Activity 4.



The cost of the stereo goes up at each stage due to the cost of production and profit. There may even be a wholesaler between the manufacturer and seller (distributor) in which case the final sale cost may even be higher. The way in which the final sale price will be determined is by attaching a profit to the **unit cost**.

*Unit cost: the cost of producing one item or product*

4. Why does the price of a good or a service go up at each step in the marketplace?

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Check your answers by turning to the Appendix, Section 3: Activity 4.

**Supply**

Supply is the amount of a good or service that a seller is willing to offer for sale. Supply is often determined by the price that consumers are willing to pay for a product. Two terms that show the importance of consumer spending on supply and demand are *dollar voting* and *consumer sovereignty*.

A sovereign is a king or queen, so consumer sovereignty means the consumer is king or queen. The consumer’s kingdom is the market, and whatever the consumer wants produced will be produced.

The reason the consumer has so much power in determining supply is partly due to dollar voting. To vote means to show support or to express an opinion.

**Dollar Voting**

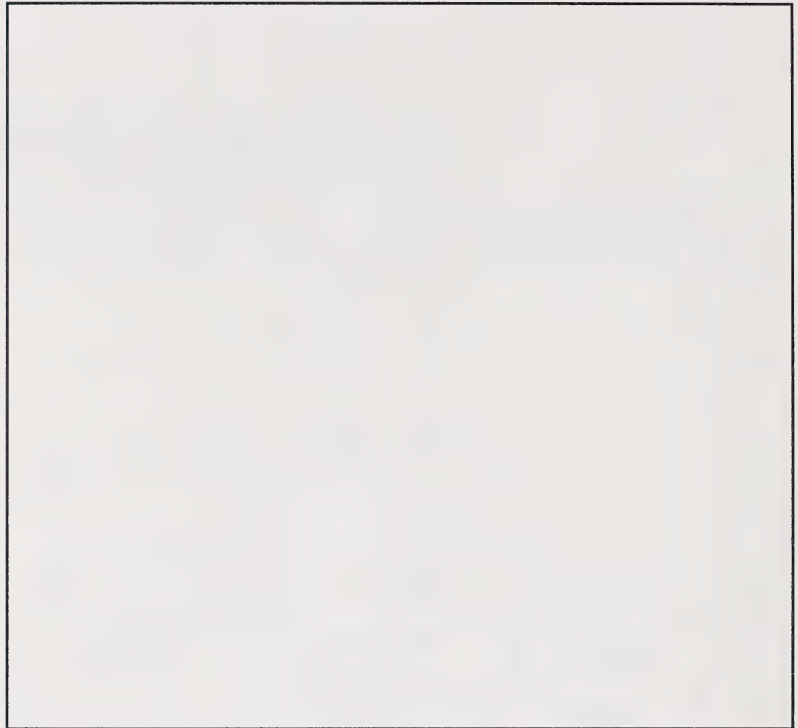
Dollar voting means to express your opinion on certain products by either using your dollars to buy or not buy a product. Those products that you demand will be supplied.

**Consumer Sovereignty**



5. In the box provided draw a picture or cartoon which shows the concept of dollar voting.

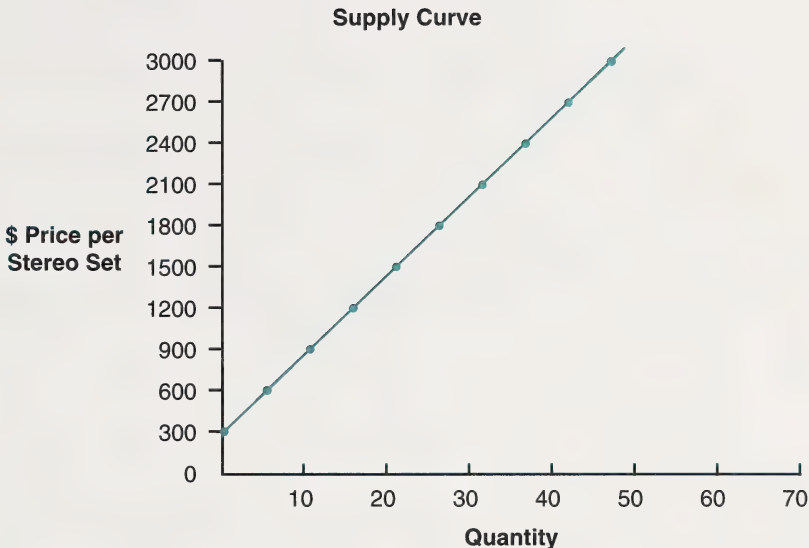
**Dollar Voting**



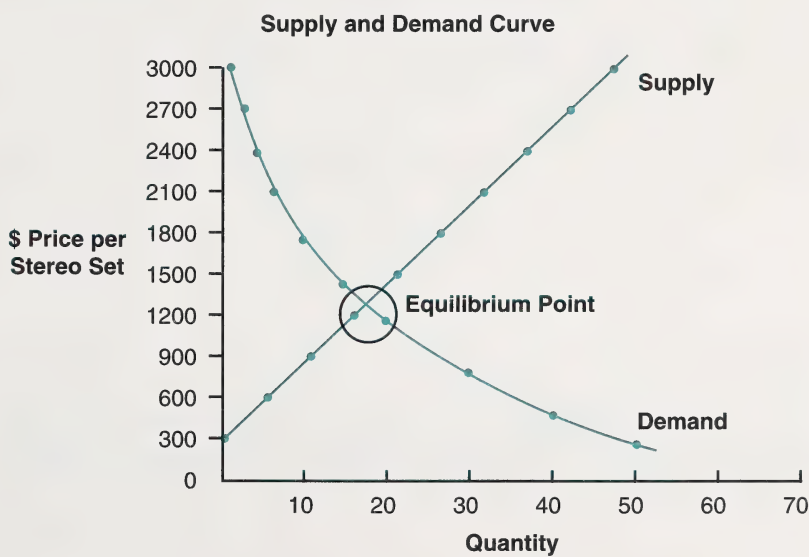
In examining supply it becomes obvious that the stereo shop owner will want to sell more stereos as the price of a stereo increases. Look at the following chart.

SUPPLY	
\$ Price	Quantity
300	1
600	5
900	10
1200	15
1500	20
1800	25
2100	30
2400	35
2700	40
3000	45





By combining the supply and demand curves using the two lists of figures, an equilibrium point can be found. This is the point at which the supply and demand curves intersect. This is where the rate of supply meets demand.



6. What is the price at the equilibrium point?
- 
7. What is the quantity at the equilibrium point?
- 
8. Suppose the seller tried to charge \$2700 per stereo. What will the demand for stereos be at that price?
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- 
9. At \$900 per stereo, what would the demand be?
- 
- 
10. There is a great demand for stereos. Fifty people are willing to buy at \$300. Will there be the supply to fill this demand? Explain.
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- 
11. Describe the effect that the private individual can have on supply and demand.
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- 
12. How do supply and demand determine **distribution** of goods and services?
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*Distribution: the division of goods and services among several or many*

Examine the cartoon and answer the question that follows.



13. The goose is discussing the concept of supply and demand. Why does the goose feel she will affect the price of gold if she lays golden eggs?

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Check your answers by turning to the Appendix, Section 3: Activity 4.

<sup>1</sup> Canadian Speakers' & Writers' Service Ltd. for the cartoon by Ben Wicks. Reprinted by permission of the Canadian Speakers' & Writers' Service Ltd.



## Activity 5: The Three Economic Questions

You will now determine how private enterprise answers the three economic questions.

### What Products or Services Should Be Produced?

This is decided by the desire or demand for a product or service. There is a limit to the amount of money you, a consumer, have. There is also a limit to the goods and services available. So, you must make a choice. What do you want to buy? If enough consumers decide that they want to buy a stereo, then stereos will be produced. If fewer consumers want to buy a stereo, then fewer stereos will be made. Whatever decision you make has an opportunity cost.

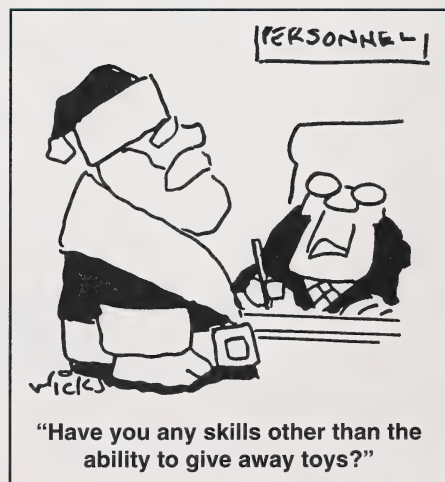
Another way of saying this is, if you buy a stereo then perhaps you cannot buy a bike. The bike is the opportunity cost. It is an alternative use of resources.

### How Should the Goods and Services Be Produced?

Remember that self-interest drives a person in business to seek a profit. Also, land, labour, and capital are scarce. So the producer must decide how to most effectively and efficiently use the three resources to produce goods or services. The least expensive way (method of production) will be chosen. This will lower the cost of production and increase the profit.

### Who Gets What Share of the Goods and Services Produced?

The question of who gets what portion of goods and services distributed to them is decided by a person's ability to buy the goods. If you have a skill which is in demand, you will be able to get a job. You may also make a good deal of money. The amount of skill involved in a job also will determine the amount of money paid in wages or salary. Some jobs do not have a high demand or skill level.



<sup>1</sup> Canadian Speakers' & Writers' Service Ltd. for the cartoon by Ben Wicks. Reprinted by permission of the Canadian Speakers' & Writers' Service Ltd.

In Section 1, you examined the need for money. In our society money is used as a means of exchange. If you want a product, you pay for it with money. When you do a job, you are paid with money. You can then go into the market and buy what you want, if you can afford it. People who earn more money can buy more goods and services.



1. What is the basis for deciding what is produced in a private enterprise economic system?

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2. How are goods and services produced in a private enterprise economic system?

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3. For whom are the goods produced in a private enterprise economic system?

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4. What is opportunity cost?

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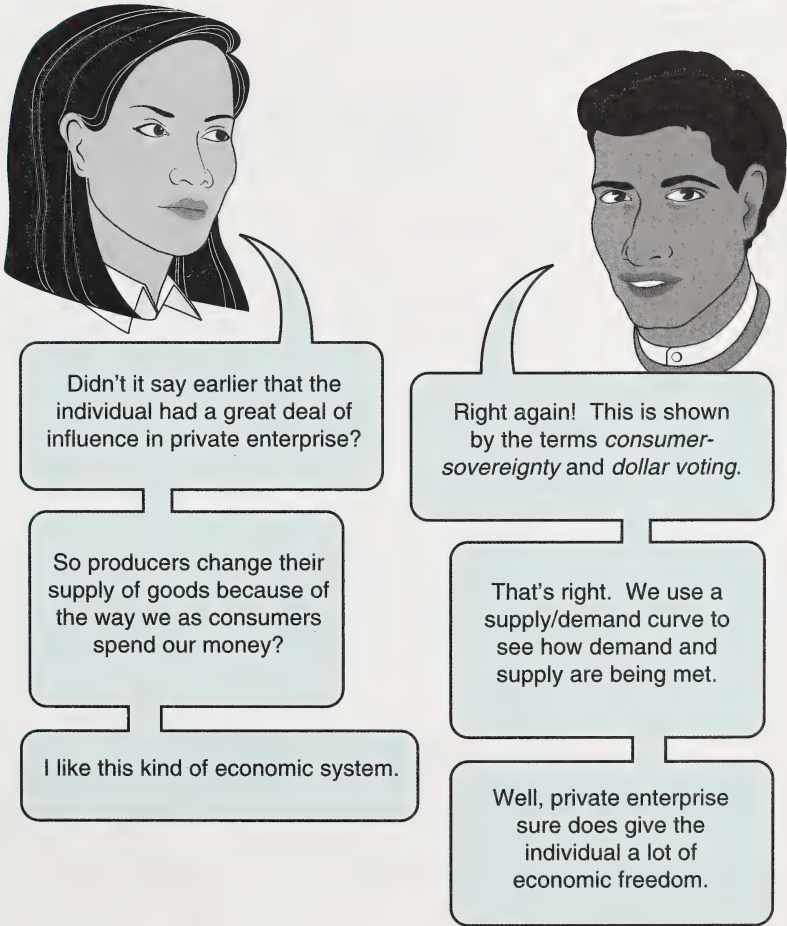
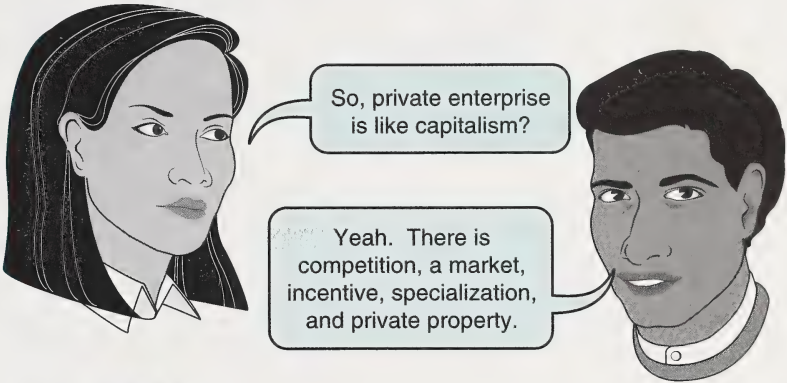
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Check your answers by turning to the Appendix, Section 3: Activity 5.



Activity 6: Private Enterprise Summary

Read the dialogue between the two people and complete the questions which follow.



Why do you think an economic system would be based on the principles of private enterprise?

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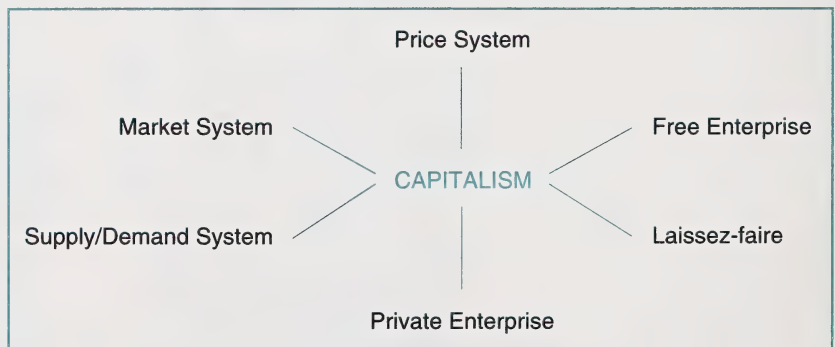
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Check your answers by turning to the Appendix, Section 3: Activity 6.

Private enterprise is just one name for an economic system based on the principles of capitalism.



### Follow-up Activities

If you had difficulties understanding the concepts in the activities, it is recommended that you do the Extra Help. If you have a clear understanding of the concepts, it is recommended that you do the Enrichment.

Extra Help

Match the following terms to the appropriate description.

- |                     |                         |
|---------------------|-------------------------|
| a. market           | f. competition          |
| b. specialization   | g. demand               |
| c. productivity     | h. supply               |
| d. private property | i. consumer sovereignty |
| e. incentive        | j. dollar voting        |

- \_\_\_\_\_ 1. something that motivates an individual to act
- \_\_\_\_\_ 2. the right of an individual to own his/her skills and possessions
- \_\_\_\_\_ 3. the belief that the consumer is king or queen (Consumers will determine the price and quality of goods they will buy.)
- \_\_\_\_\_ 4. being able to concentrate on performing a specific job or skill
- \_\_\_\_\_ 5. voting for the products by buying them
- \_\_\_\_\_ 6. the amount of a good or service made in relation to the cost of production
- \_\_\_\_\_ 7. the amount of goods or services producers (sellers) are willing to offer for sale
- \_\_\_\_\_ 8. the degree to which consumers are willing (or desire) to buy a product or service
- \_\_\_\_\_ 9. the act of competing in a market
- \_\_\_\_\_ 10. a set of arrangements whereby buyers and sellers meet to exchange goods and services for some form of money

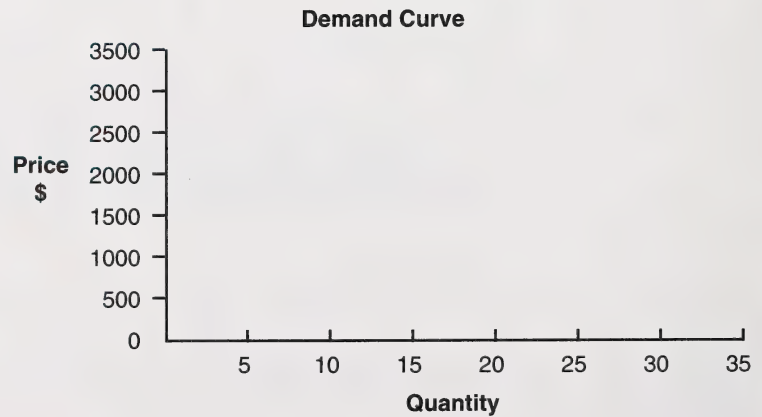
Check your answers by turning to the Appendix, Section 3: Extra Help.

Enrichment

You are provided with a supply schedule and a demand schedule. You must plot the numbers on to a supply/demand curve and find the equilibrium point.

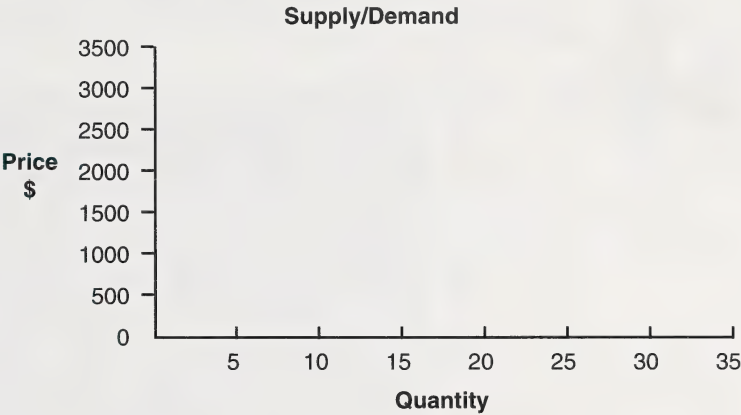
SUPPLY SCHEDULE		DEMAND SCHEDULE	
Price \$	Quantity Produced	Price \$	Quantity Produced
500	1	500	30
1000	5	1000	25
1500	10	1500	20
2000	15	2000	15
2500	20	2500	10
3000	25	3000	5
3500	30	3500	1

1. First plot the numbers on separate supply/demand curves.





2. Now take both the supply and demand curves that you have done and place them on the following graph.



3. What is the price of the good or service at the equilibrium point?

\_\_\_\_\_

4. What is the quantity supplied at the equilibrium point?

\_\_\_\_\_

Check your answers by turning to the Appendix, Section 3: Enrichment.

### Conclusion

The way in which a country attempts to answer the three basic economic questions will determine its economic system. If freedom of the individual and private property are considered important, then private enterprise – or any of the other names for capitalism – will be the economic system. If group security, equality, and cooperation are highly emphasized in a society, then the economic system will be more socialist than capitalist.

### ASSIGNMENT

There is no assignment for this section.

# Capitalism in Practice



**W**hat news about the economy makes the headlines? What are some of the major economic concerns people have at present? How does the business community feel about the times – are things promising or are there signs of an economic downturn? Much like life in general which has its ups and downs, business goes through cycles that result in economic ups and downs. If you have an opportunity to talk to some of your elders, ask them about the 1929 stock crash and the Depression of the 1930s. Even though this happened many years ago, it is significant since changes were made to the capitalistic economic system because of these events.

**P**ure capitalism in its traditional form encountered problems. Some of these problems, as well as solutions to these problems, will be examined in this section. The subsequent changes that capitalism encountered further developed the idea of a mixed economy.

**I**n this section you will

- understand basic problems with pure capitalism
- identify the need for adaptation in capitalism
- solve an economic problem
- understand basic Keynesian economics

## Activity 1: Emerging Problems of Capitalism

Capitalism in theory has a very limited role for government. This role is to keep the market peaceful and secure for competition. Read the following article.

### Statscan makes \$500 million error

by Drew Fagan

#### Ottawa

Statistics Canada had egg on its face yesterday as it admitted that information released this week on Alberta's expected deficit was wrong by \$500 million.

The agency reported on Monday that Alberta's deficit for the fiscal year that began April 1 was going to be \$2.2 billion—a figure that shocked provincial politicians and quickly led to some anxious phone calls to Ottawa from Alberta Treasury officials.

Statscan officials reviewed their work and soon found mistakes had been made in calculating the Alberta deficit, and that it actually should have been

pegged at \$1.7 billion.

That still gives Alberta the largest financial shortfall of any province by a wide margin—with Quebec following at \$955 million.

In order to calculate the provincial deficit estimates, a complicated formula is used by Statscan to correlate figures from provinces that utilize different accounting methods.

Statscan official Bob Sauve said yesterday that in doing so, some out-of-date figures from Alberta were used, throwing the final figure out of whack.

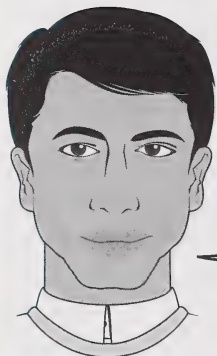
"It's a complicated area and there's a realization of that," he said. "But it's still unfortunate."<sup>1</sup>

1. What did Statistics Canada give as its updated deficit for Alberta?

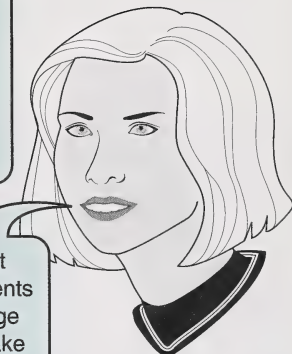
Check your answers by turning to the Appendix, Section 4: Activity 1.

If government is not supposed to be involved in the economy, then how did the Alberta government build up a 1.7 billion dollar deficit? Where did it spend this money in the economy, and why did it feel that it even had to spend the money?

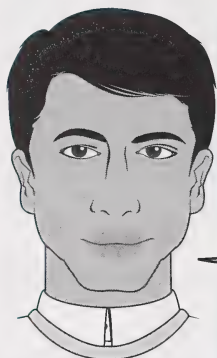
<sup>1</sup> *Globe and Mail* for the article "Statscan makes \$500 million error," July 15, 1989, 29-B1. Reprinted by permission of *Globe and Mail*.



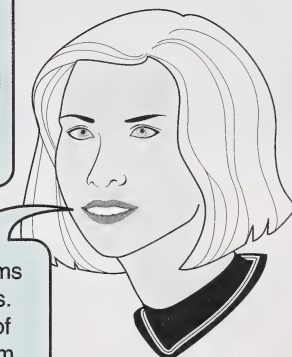
I thought government was not supposed to get involved in a capitalist economic system. This news article shows they are involved to a great extent.



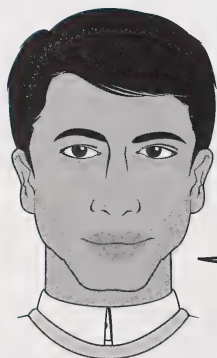
Well, you are right. But times change. Governments have to adapt and change economic systems to make sure that they fulfill the needs of society.



O.K. That makes sense. But then you can't say that an economy where the government gets this involved is still capitalism. And, just how much government intervention is too much?



This is why economic systems today are mixed economies. They have characteristics of both socialism and capitalism. To answer your question, I don't know how much government intervention is needed.



Let's see. The first question we wanted to look at was: What were the problems that developed with capitalism, causing a need for change and adaptation?



## Problems with American Capitalism

Problems did emerge under a capitalist economic system. The ideas of individualism and economic Darwinism were carried to extremes in the United States prior to the Depression. A small number of men, such as J. D. Rockefeller and J. P. Morgan, were becoming extremely wealthy. This small group of men monopolized the wealth and economic power in the United States. They were able to control large sections of the economy because of their shrewd business dealings. Many people were upset over this accumulation of wealth by such a small number. After all, capitalism was supposed to be left up to the actions of individuals interacting in the free market, not to a small group of wealthy “robber barons.” The mood of a large number of Americans concerning these “robber barons” was expressed by a senator by the name of Huey Long.

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All the people of America have been invited to a barbecue. God invited us all to come and eat and drink all we wanted. He smiled on our land and we grew crops of plenty to eat and wear.

He showed us the earth, the iron, and other things to make anything we wanted. He unfolded to us the secrets of science so that our work might be easy. God called: ‘Come to my feast.’ Then

what happened? Rockefeller, Morgan, and their crowd stepped up and took enough for 120,000,000 people and left only enough for 5,000,000, for all the 125,000,000 to eat. And so many millions must go hungry and without these good things God gave us unless we call on them to put some of it back.

I call on you to organize Share Our Wealth societies.<sup>1</sup>

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The monopoly of power by a small number of men created a centralization of the economic decision-making power. This was, of course, opposite to the capitalist view that decision making should be decentralized – with many individuals in the market.

2. Who were the “robber barons”?

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<sup>1</sup> Longman Group Limited for the excerpt from *Twentieth Century, The World Since 1900*, Second Edition. Tony Howarth, Longman House, Burnt Mill, England, 1987 pg. 124.

3. Why were many people upset with men such as J. D. Rockefeller and J. P. Morgan?

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4. How did the emergence of the “robber barons” go against the principles of pure capitalism?

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5. Does capitalism encourage the development of “robber barons”? Explain.

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Check your answers by turning to the Appendix, Section 4: Activity 1.

## Activity 2: An American View of Poverty

*Poverty: a lack of money and possessions needed to supply life's basic needs*

The accumulation of wealth by a few, such as Rockefeller and Morgan, meant **poverty** for many.

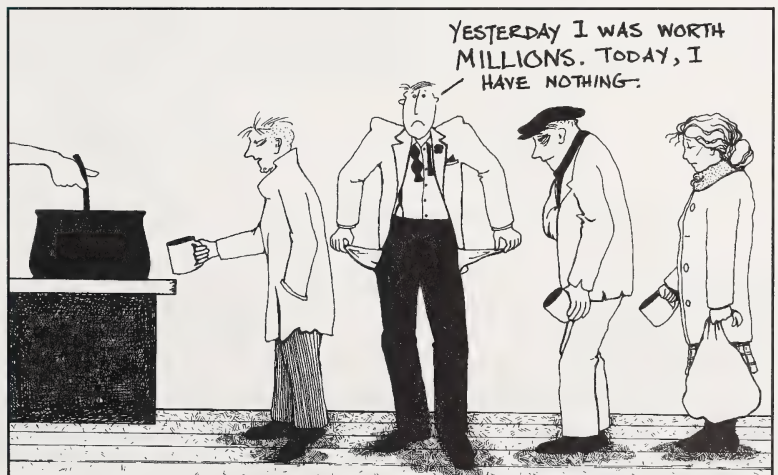
The ideas of economic Darwinism and individualism meant that some people would do well and others would not, but a large number of people in the United States were not prepared to lead a life of poverty to benefit the rich.



During the 1930s thousands of people "rode the rails" across Canada looking for work.

The attitude which was evident in the United States and Canada prior to the Depression in 1929 was beginning to change. No longer was poverty a definite sign of weakness and failure, but instead poverty became a sign of difficult times and exploitation by the "robber barons."

This was not true just because of the poor becoming more vocal, but also because many wealthy people were losing everything they had. People who had been rich before the stock crash in 1929 were left penniless with the coming of the Depression. The strongest did not always survive. Some of the ideas that had formed the backbone of capitalism were being questioned. People needed help, and many people started to look to the government to provide that help.



1. What is poverty?

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2. How did the perception of poverty change because of the stock crash and Depression?

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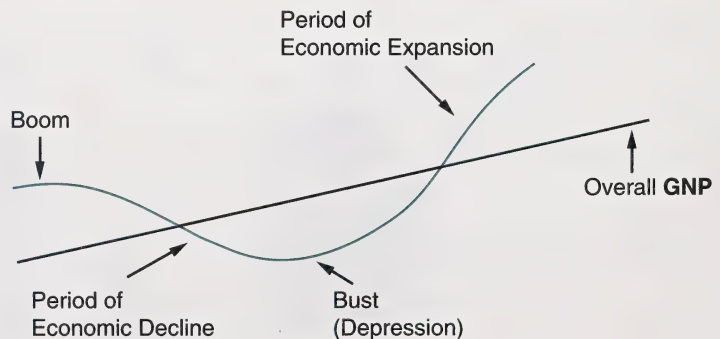
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Check your answers by turning to the Appendix, Section 4: Activity 2.

### Activity 3: The Business Cycle

One of the major problems capitalist nations must constantly deal with is an economic event known as the business cycle. This means that the economy will go through periods of boom (good times) and bust (bad times). In the United States there was a boom during the 1920s.

The decade of the 1920s was referred to as the “roaring twenties.” The economy was doing well; people were spending money and they were happy. But the stock market crash of 1929 signalled an end to the boom. The business cycle had encountered a major problem for which it did not seem to have answers.



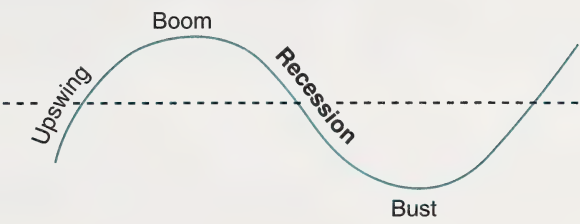
*GNP: gross national product, the total value of all goods and services produced in a country in one year. It is hoped a steady moderate increase will occur in a given year.*



Some people began to see a need for the government to step in and do something about the economy in order to achieve a more stable situation. The goal would be to achieve a moderate rise in the GNP as shown on the chart. This could be accomplished by eliminating the huge peaks (booms) and valleys (busts).

Examine the following information to help you further understand the business cycle.

***Recession:** a temporary falling off or slowing of business activity*



"Boom" Characteristics	"Bust" Characteristics
<ul style="list-style-type: none"><li>• full employment</li><li>• high inflation</li><li>• high investment</li><li>• high demand</li></ul>	<ul style="list-style-type: none"><li>• high unemployment</li><li>• low inflation</li><li>• low investment</li><li>• low demand</li></ul>

1. What is an economic boom?

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2. What is an economic bust?

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Check your answers by turning to the Appendix, Section 4: Activity 3.

One of the effects of an economic bust or depression is unemployment. Unemployment during the Depression shot up to unbelievably high rates.

UNEMPLOYMENT IN THE USA, 1929–32		
Year	Number of Unemployed People	Unemployed as % of the Labour Force
1929	1 550 000	3.2%
1930	4 340 000	8.7%
1931	8 020 000	15.9%
1932	12 060 000	23.6%

The result of this extremely high rate of unemployment was an unhappy and desperate population.

3. What was the percentage of unemployed at the beginning of the Depression?

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4. How many years did it take for the unemployment rate to reach 23.6%?

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Check your answers by turning to the Appendix, Section 4: Activity 3.



But couldn't capitalism work its way out of the Depression?

The American president at the time of the Depression, Herbert Hoover, had offered very little government aid. He instead had hoped that the traditional capitalist economic system would revive itself without too much help. Hoover did not want to spend too much money helping the economy because he wanted a balanced budget. Interest rates were raised to discourage investment rather than lowered to encourage spending and investment. This point will be covered in more depth later in this section.

<sup>1</sup> Longman Group for the chart from *Twentieth Century History, the World Since 1900*, Second Edition. Tony Howarth, Longman House, Burnt Mill, England, 1987, p. 101.

## Activity 4: Roosevelt and the New Deal

Problems within the capitalistic economic system were clearly evident – poverty, monopolies, unemployment, and above all, the Depression. In 1932 the American people elected a president who was offering the electors and the nation a “New Deal.” His name was Franklin Delano Roosevelt.

In this activity you will be asked to solve a problem related to government intervention in the economy. Follow the steps outlined to help you find solutions to this problem. You will be expected to complete a final assignment on the New Deal in your Assignment Booklet.

Problems are something that everyone faces from time to time. One of the keys in life is to be able to successfully overcome problems. It helps to have a strategy to work through problems or handle difficult questions. The following is a model for problem solving. The model has four steps and will be used to help you answer two questions. In this part of the section you are expected to work through each step of the problem-solving model.

### A Model for Problem Solving

**Step 1:** Understand the Problem

**Step 2:** Develop Research Question, Form Hypothesis

**Step 3:** Gather and Organize Information

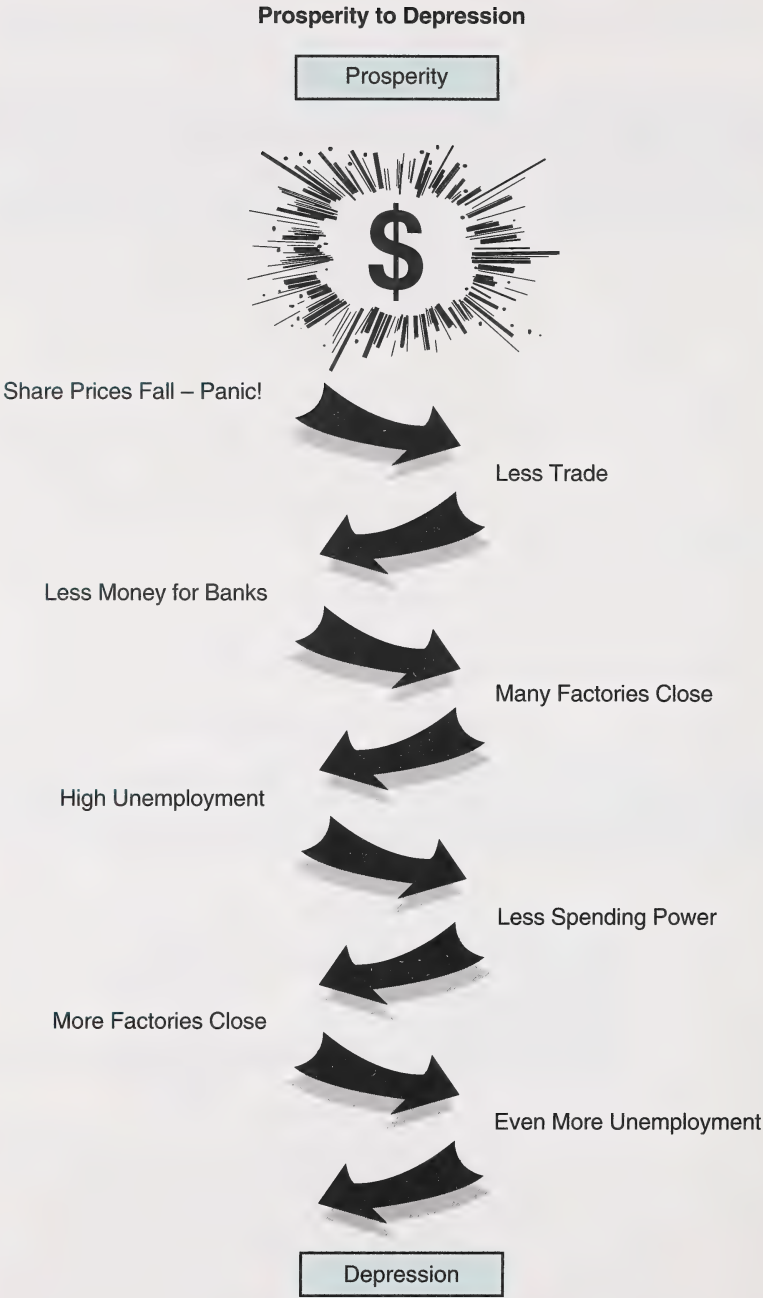
**Step 4:** Develop a Conclusion

You will use the following question as a focus for your problem solving.

**Why did the American government implement the New Deal in the 1930s?**

### Step 1: Understand the Problem: Depression – U.S.A. 1929

To see how the Depression began, you can examine the illustration that follows. Prior to the Depression, times had been good in the “roaring twenties.” Many people had invested in stocks because they could buy stock with only a 10% down payment. As a result, one could buy \$1000 worth of stock for \$100. This led to a serious overextension of credit. In other words, people owed a great deal on these stocks. When the stock crash occurred, the investors lost everything. Then the banks, who had often loaned investors the money, came calling for their money and investors could not pay. The spiral to depression had started, and it could not be stopped.



Confidence in the economy and the government was at an extremely low level. Something had to be done to increase employment, consumer spending, and confidence in the economy.



1. What is overextension of credit?

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2. How does unemployment affect consumer spending?

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Check your answers by turning to the Appendix, Section 4: Activity 4.

**Step 2: Develop Research Questions, Form Hypothesis**

When you go about problem solving, you are expected to tackle the overall questions in a systematic and organized fashion. In this step of the model, you must decide what information needs to be acquired in order to answer the question for study: Why did the American government implement the New Deal in the 1930s? However, when you work as a researcher, it is expected that you ask or formulate questions that will be used as the basis for answering your overall question.

The following are suggested examples of some research questions that will help you answer the overall question.

- What was the New Deal?
- How did the New Deal work?
- Who introduced the New Deal?

3. Use the “five Ws” (Who? What? Where? When? Why?) to develop three more research questions that will help you answer the main question.

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4. At this time you should review the model for problem solving. Then write a hypothesis (an educated guess as to the answer) for the overall question:

**Question: Why did the American government implement the “New Deal” in the 1930s?**

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Check your answers by turning to the Appendix, Section 4: Activity 4.

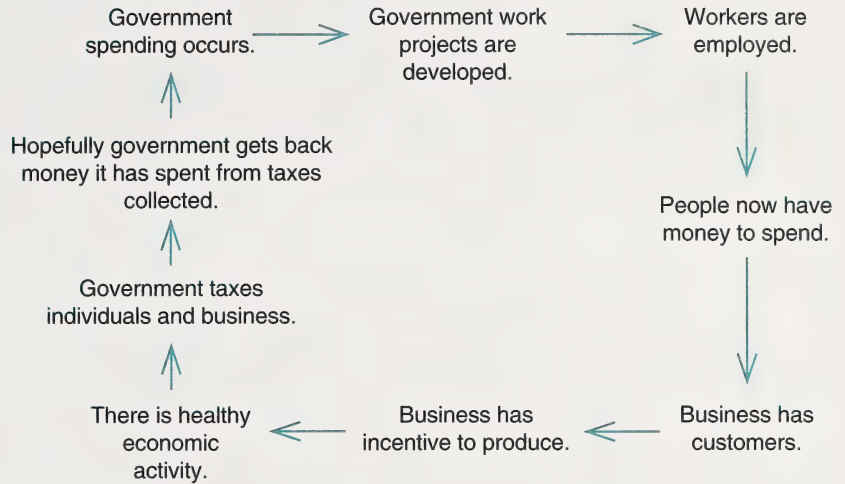
### Step 3: Gather and Organize Information

When gathering and organizing your information, you are attempting to develop a base of knowledge. This base of knowledge will assist you in answering your research questions and ultimately in answering the overall question. It is important that your information be as accurate as possible. Before selecting the method for completion of Step 3, return to your list of research questions and use them as the starting point for gathering your information. In order to successfully complete this step, each of the research questions will have to be answered. To gather and organize information for this step, read the following:

The American people elected Franklin D. Roosevelt because they were prepared to try anything to break out of the Depression. Roosevelt began immediately and over the first one hundred days in office he set up a number of “alphabet” agencies. These agencies were going to be used to put people back to work.

The goal of these programs was to get the American economy back on its feet. To do this, Roosevelt had to spend money. He felt that by using capital work projects to employ people the economy would grow strong and the flow of money would begin again.

### Government Spending Cycle



Here is a brief description of Roosevelt's actions.

In his first "100 Days" as President, Roosevelt asked for and got from Congress an extraordinary burst of activity – making laws, voting money for new government programmes, setting up new agencies to carry them out. The first of the "alphabetical agencies" appeared – the organizations through which Roosevelt would tackle the Depression – the CCC, the NRA, the AAA, the PWA, the TVA. In 1934 more agencies were set up, and yet more still in 1935. The list seemed endless; to some people the rows upon rows of initials were confusing – FERA, CWA, RA, FCA, WPA, NYA, REC, NLRB. And to other people they seemed, somehow, 'un-American', and with more than a tinge of socialism.

In 1935 former President Herbert Hoover would declare:

"There are only four letters of the alphabet not now in use by the administration. When we establish the Quick Loans Corporation for Xylophones, Yachts and Zithers, the alphabet of our fathers will be exhausted. ...But, of course, the new Russian alphabet has thirty-four letters."

But for millions of Americans, who remembered all too vividly the dispiriting years when Hoover was president, these new agencies represented action instead of empty words. For many people they represented relief from starvation, the chance of a job and holding on to the family home: for some they meant the difference between life and death.<sup>1</sup>

<sup>1</sup> Longman Group for the excerpt from *Twentieth Century History, The World Since 1900*, Second Edition. Tony Howarth, Longman House, Burnt Mill, England, 1987, p.119.

This government activity of direct involvement in the economy is contrary to the principles of capitalism, but as you have read, many American people demanded government action. However, there was so much government involvement and intervention in the form of these agencies that some people began to say that Roosevelt was not a true capitalist. This was perhaps true. Roosevelt was concerned with group welfare, and he did see a need to alter capitalism to meet the needs of the time. Government in the United States under Roosevelt became an active participant in the economy during the difficult times of the Depression. There was a feeling that things were moving again. The American people responded positively to Roosevelt's actions.

He listened to the advice of his “brain trust” – the university teachers he brought into the business of government – and developed policies that would relieve misery and that might turn the American economy around. Roosevelt's confident mood was catching. The head of Thomas A. Edison Inc. posted this notice on the walls of his firm in New Jersey:

President Roosevelt has done his part: now you do something.

Buy something – buy anything, anywhere, paint your kitchen, send a telegram, give a party, get a car, pay a bill, rent a flat, fix your roof, get a haircut, see a show, build a house, take a trip, sing a song, get married.

It does not matter what you do – but get going and keep going. This old world is starting to move.

5. Why was Roosevelt not considered a true capitalist by some?

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Check your answers by turning to the Appendix, Section 4: Activity 4.



Use the following information to answer the questions that come after.

### Roosevelt's New Deal

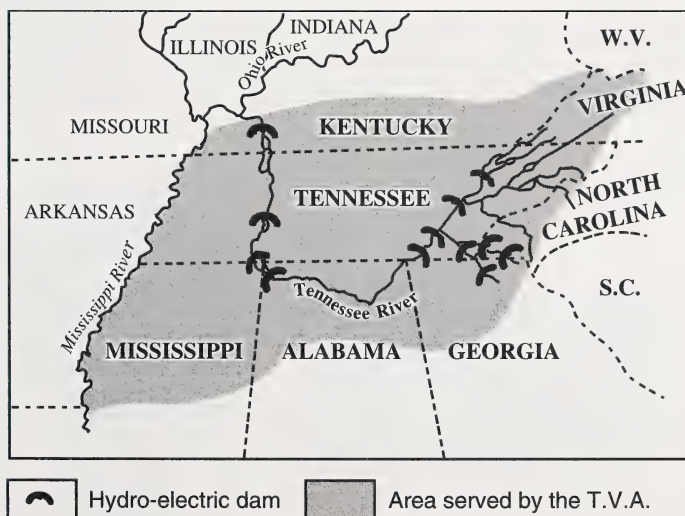
Because President Hoover had no solution to the breakdown in the American economy, the American electors voted for his Democrat rival, Franklin D. Roosevelt in the 1932 elections. Roosevelt's answer to unemployment was a "New Deal" which included the following:

- federal aid to the 48 states
- social security; i.e., unemployment and sickness pay
- 'work-finding' schemes such as irrigation projects, and bridge and dam construction (The Tennessee Valley Authority, a plan that boosted agriculture and industry in several states, was the most famous.)

Roosevelt faced a great deal of opposition from political opponents who disliked his interference in affairs of individual states. However, the American people were behind him, and Franklin D. Roosevelt remained in office for the next three presidential elections.

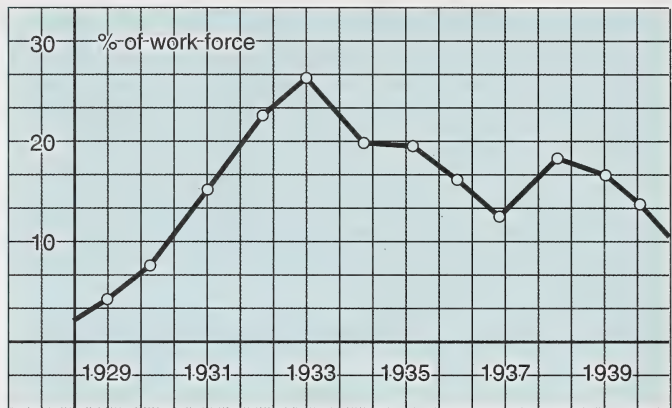
### Some Parts of the New Deal

- T.V.A. (Tennessee Valley Authority): It transformed the valley from poverty to prosperity over an area of 65 000 square kilometres. It involved hydro-electric power, irrigation, new industries, and work training.



- C.C.C. (Civilian Conservation Corps): Two and one-half million unemployed young Americans were given jobs in forestlands.
- P.W.A. (Public Works Association): Useful work for the unemployed was created with over three billion dollars assigned for national construction projects.
- H.O.L.C. (Home Owners Loan Corporation): People who would have lost their homes were loaned money to maintain their mortgage payments.

**United States Unemployment, 1929–1940**



6. What roles did the government under Roosevelt take regarding capital works projects?

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7. Did Roosevelt have any success with his programs in lowering unemployment? Explain.

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8. One American voter said: “Roosevelt is the only President who has ever cared for people like us.” Why would people feel this way?

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Check your answers by turning to the Appendix, Section 4: Activity 4.

#### Step 4: Develop a Conclusion

The final step of the problem-solving model is to develop conclusions. Look at the New Deal and try to conclude why the government of the United States implemented the New Deal in the 1930s. This will be your assignment for this section.

#### Activity 5: Keynesian Economics

One of the most brilliant economists of this century was John Maynard Keynes. He was born in 1883 in England. He led a very distinguished career as a professor of economics at Cambridge University.

Keynes developed some unique economic theories. They were so unique, in fact, that his ideas became known as Keynesian Economics. These ideas along with the New Deal under Roosevelt caused the capitalist economic system to adapt to changes in society.



What was government's role in an economy, according to Keynes?

*Tradition: a belief or practice that has been handed down from previous generations*

When a **traditional**, or pure capitalist, economy is working well, there is little need for a government to get involved. As stated in Section 2, it must ensure competition and a peaceful market. However, when times are bad, as during the Depression, Keynes' ideas called for the government to take a very active role—a role very similar to the one taken by Roosevelt under the New Deal.

Keynes felt that strong government spending would get the economy going again. He felt that a lack of consumer spending had been a major cause of the Depression, so if the government got people working and spending, the economy would have to improve. The increased consumer spending would raise demand for goods and services which would increase production.

1. When did Keynes feel a government should get involved in the economy?

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2. Why did Keynes feel a government should get involved in the economy?

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3. Name one way in which Keynesian Economics and the New Deal were similar.

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Check your answers by turning to the Appendix, Section 4: Activity 5.

*Fiscal policy: a policy dealing with government spending and taxation*

*Monetary policy: a policy having to do with the amount of money in circulation in the economy*

There are two specific economic policies which Keynes felt could and should be employed by governments to help their economies avoid depression. They are **fiscal** and **monetary policies**. All economies have these policies, but they differ in the way in which they are used.



*Disposable income: money left over after taxes have been paid*

Fiscal policy refers to the government's role in collecting taxes and spending money. Under fiscal policy the government has the ability to increase or decrease taxation. In difficult times – a recession or depression – the government could decrease taxation. This would result in the people of the country hanging on to more of their money. The money that is left to a person after taxation is called **disposable income**. The more money or disposable income people have usually encourages growth of the economy.

During times of inflation, the government could raise taxes which would help to slow the rate of consumer spending. This will cause the upward trend of consumer prices to stabilize.

Keynes felt that monetary policy could also be used to ensure a stable economy. Under monetary policy the government has the power to control the amount of money available in the economy. This can be accomplished by increasing or lowering interest rates. If you lower the interest rate at banks, people are less likely to keep their money there. If they are discouraged from saving their money, they must find something else to do with it. Consumers may decide to spend this money or invest it in the economy. At the bank you might only be earning 6% interest which may cause you to withdraw your money because you may feel that through your own investments you could receive a 10% return on your money.

By lowering interest rates the government makes it more attractive to borrow money. You will be more likely to take out a loan to buy a stereo if the interest rate is 6% rather than 10%. This will also increase consumer spending which will strengthen the economy. These policies can be used to make sure a country does not enter a recession or depression, or they can be used to get a country out of bad times.

*Inflation: a time of generally rising prices  
This will then cause a decline in the purchasing power of the dollar*

The opposite of a slow and depressed economy is one that is encountering rapid growth. If this growth is too quick, inflation may occur. The possibility of **inflation** is a major threat in all capitalist economic systems. During a period of economic expansion (refer to the drawing of boom/bust cycle) it is hoped that there will be a moderate increase. Growth that is too fast could result in inflation.

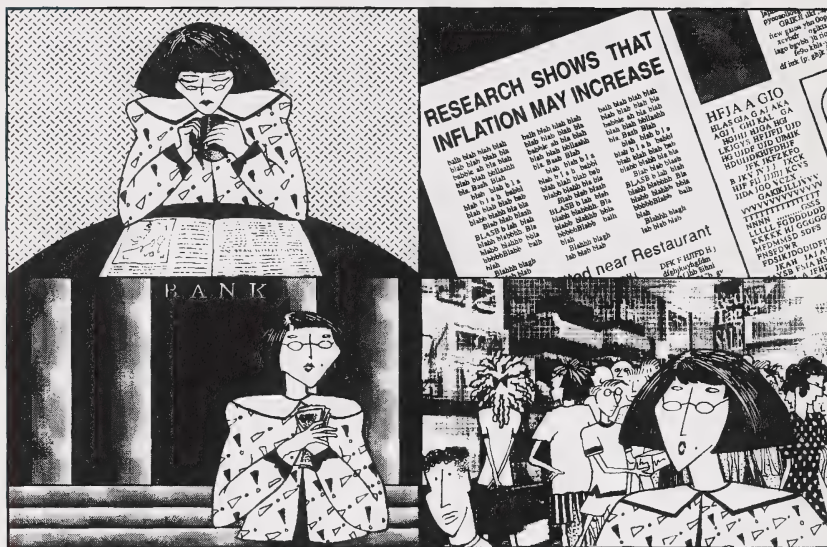
There are three general causes of inflation: expectation, demand-pull, cost-push.

## Expectation

When people expect inflation to occur, they tend to contribute to it.

They will spend their money today for fear that it will be worth less tomorrow. Because they increase their spending, they create higher demand for goods and services which raises prices.

### Expectation



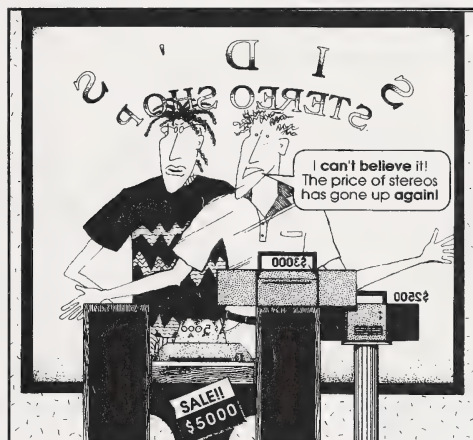
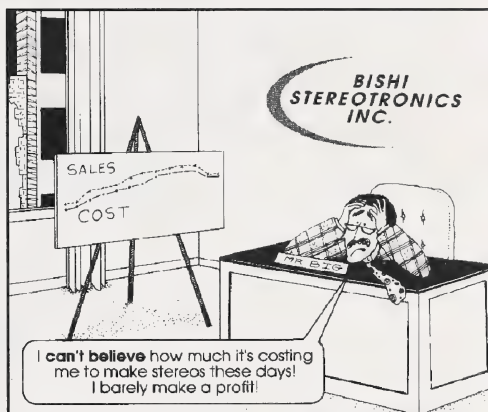
### Demand-Pull

This cause of inflation is similar to expectation in the sense that there is an increasing demand for a product. If 1000 people want to purchase a stereo, yet there are only 100 stereos for sale, the seller will be able to demand a very high price. The stereos will eventually be sold to those 100 people willing to pay the most for the stereos.



## Cost-Push

The final cause of inflation is cost-push. If there is a period of economic expansion, workers may ask for a wage increase to pay for the higher prices of goods and services caused by increasing demand. Because times are generally good, manufacturers may grant the wage increase. Remembering their own self-interest though, the manufacturers are going to want to maintain a profit margin, so they will most likely raise or push-up the price of the product. The reason the manufacturers do this is to keep up with the rising “costs” of production. The costs of production, as stated earlier, might be the wages of the workers, but it might be any rise in the price level of any resource the producer may use in production.



4. What is inflation?

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5. Describe expectation as a cause of inflation.

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6. Describe demand-pull as a cause of inflation.

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7. Describe cost-push as a cause of inflation.

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Check your answers by turning to the Appendix, Section 4: Activity 5.



So how has capitalism been affected by Keynesian economics?

## Activity 6: Keynes on Trial

Read the following article and then answer the questions that come after it. You may also listen to the audiotape that goes with the reading. Note that the article is dated 1983, so some world leaders have changed since it was written.



### ===== The Case of Capitalism versus Keynes =====

*Politicians have used the theories of John Maynard Keynes to build a mixed economy. Freelance writer Bruce Gates creates a fictional trial in which an out-and-out capitalist accuses Keynes of destroying free enterprise.*

John Maynard Keynes is on trial. Keynes (1883–1946) was the British economist credited with rescuing capitalism from disaster during the Depression of the 1930s. One of his ideas was that governments should spend more than their income to stimulate growth during hard times. This idea has dominated economic planning for several decades; now it is coming in for heavy cross-examination. Have politicians carried Keynesian theory too far? Read the mock trial below and

judge for yourself.

**Prosecutor:** Mr. Keynes, you stand charged with creating this mixed-up economy of ours.

**Keynes:** You mean *mixed* economy. All capitalist countries have mixed economies to varying degrees, combining free enterprise with government controls. And this is as it should be.



**Prosecutor:** Is it really?

**Keynes:** Precisely. During high unemployment and slow growth, governments should increase spending to get the economy moving. When the economy recovers, governments should step aside; keeping an eye on things from afar.

**Prosecutor:** But governments haven't done that, Mr. Keynes. Instead, they have created bloated bureaucracies and red tape for business – all because of your ideas.

**Keynes:** I'm afraid you give undue credit to my theory on employment, interest and money. Since the late 19th century, government involvement in capitalist economies has grown steadily. Britain in 1910, for example, introduced a social insurance scheme funded by taxes. This was done to aid people who needed help when capitalism wasn't doing its job.

**Prosecutor:** You have broken Adam Smith's cardinal rule. He stated in *The Wealth of Nations* in 1776 that free enterprise is the best way to protect the people. He stated clearly that governments only waste money.

**Keynes:** True. But you conveniently forget two things. First, Adam Smith was writing for simpler economic times. Second, Smith's theory of capitalism saw consumers gaining the most benefits, not business. In fact, Smith didn't trust businessmen, believing them to be greedy and interested in only one thing – profits through monopolies. To work properly, free enterprise has to be totally flexible to allow the supply of goods to create its own demand. This, of course means that prices, wages, and interest rates must all be free to rise, or fall, in order to encourage businesses to create jobs for everyone. This only works as long as any one group does not grow

large enough to play around with the natural law of supply and demand. Unfortunately, prior to the Stock Market collapse of 1929, greed got in the way. The whole capitalist system came crashing down around everyone's ears.

**Prosecutor:** So, you sold politicians on your theory.

**Keynes:** Politicians liked my theory because it worked for them, and they have employed it to varying degrees. President Franklin Roosevelt in the United States used massive public spending on public works projects during the 1930's. He also slapped credit regulations on the banks and stock markets. His actions restored peoples' faith in capitalism.

**Prosecutor:** And today we have a welfare state. We have governments running health care and pension plans, providing subsidized education, distributing unemployment insurance, and propping up industries that should have died years ago. This is no longer 1929, Mr. Keynes. These devices have no place in a capitalist economy.

**Keynes:** You are right. This is not 1929. But 1929 changed a lot of minds about capitalism as it was then. However, my theory really didn't take hold until after World War II, when politicians used it to restart economies stalled by the war effort.

**Prosecutor:** Your theory has created an economic monster and politicians should abandon it.

**Keynes:** That, sir, would be political suicide. Even British Prime Minister Margaret Thatcher, for all her bluster about cutting the size of Britain's welfare state, wouldn't dare dismantle it totally. There would be riots in the streets if she did. Most politicians today – even Thatcher and America's Ronald Reagan

– realize that you need some kind of economic planning by government, which is as I advised.

**Prosecutor:** Don't you think capitalists can resolve our economic mess?

**Keynes:** No. Not by themselves, I have always believed in free enterprise, but capitalists are concerned with long-term economic planning only as it benefits their businesses. Planning for an entire country can only be done through a democratic public service.

**Prosecutor:** This has led to socialist takeovers in countries such as France.

**Keynes:** No it has not! France in particular has had a long tradition of government-directed economic planning. Even before the current president, Francois Mitterrand, nationalized the banks and private companies, the French government has had its finger in the economic pie. Former President Charles de Gaulle imposed the largest program of nationalization in France's history after the second war. As a result, the French government owns Renault, the car maker; the aerospace and steel industries and telecommunications.

**Prosecutor:** And you don't think capitalism could have done it better?

**Keynes:** No. Not when big risks are involved. That's Mitterrand's concern now. He wants France to develop a strong high-technology sector because he knows this is where the future is. But to do this, the French government will have to put up the risk money, through loans to companies from the nationalized banks.

**Prosecutor:** It will never work.

**Keynes:** Perhaps it won't. But it did in Japan – now there's a good example of economic planning. The Japanese have built the mightiest economic machine on earth outside the United States, partly because they have economic planning built right into their political system.

**Prosecutor:** Explain yourself, Mr. Keynes.

**Keynes:** They used the consensus approach. Before drawing up an economic blueprint, they consult with industry, labour, the banks, universities, even the media. So, when they plan a major economic policy, it already has widespread support among the key people.

**Prosecutor:** I see little evidence in what you say of government involvement in Japan's economy.

**Keynes:** But there's plenty. As I have said, government has a key role to play in support of business. And this is what Japan does. It takes the risk for all expensive or long-term research and development. It provides private companies with up to 50% of the R and D costs, with low-interest loans from the government-owned Japan Development Bank. In return, the industry turns over the patent rights to the government-run Ministry of International Trade and Industry, which sells the technology to other private Japanese companies for a small royalty.

**Prosecutor:** That's socialism!

**Keynes:** No, that's the *mixed* economy.<sup>1</sup>

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<sup>1</sup> *Canada and the World* for the article, "The Case of Capitalism versus Keynes," November 1983. Reprinted by permission of *Canada and the World*, Waterloo, Ontario.

1. Why is John Maynard Keynes being put on trial?

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2. What was the golden rule of Adam Smith that the prosecutor said Keynes had broken?

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3. In Keynes' response to the previous question, what two things did he say the prosecutor had forgotten?

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4. According to Keynes, capitalists are concerned with long-term planning for their businesses. Who must be responsible for long-term economic planning for a country?

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5. What is a mixed economy?

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6. Would you find Keynes guilty of destroying free enterprise? Defend your position.

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Check your answers by turning to the Appendix, Section 4: Activity 6.

Activity 7: Reaganomics

Ronald Reagan was president of the United States for most of the 1980s. He spent his presidential energy focusing on a few targets that were mainly economic in nature. Thus came the term *Reaganomics* implying some new form of economic policy. Although the term *realignment* is usually used to describe political shifts, in the 1980s the key areas of economic policy underwent an economic realignment or shift. Reagan’s economic policies showed that the Keynesian idea that government deficits do not necessarily cause inflation was correct.

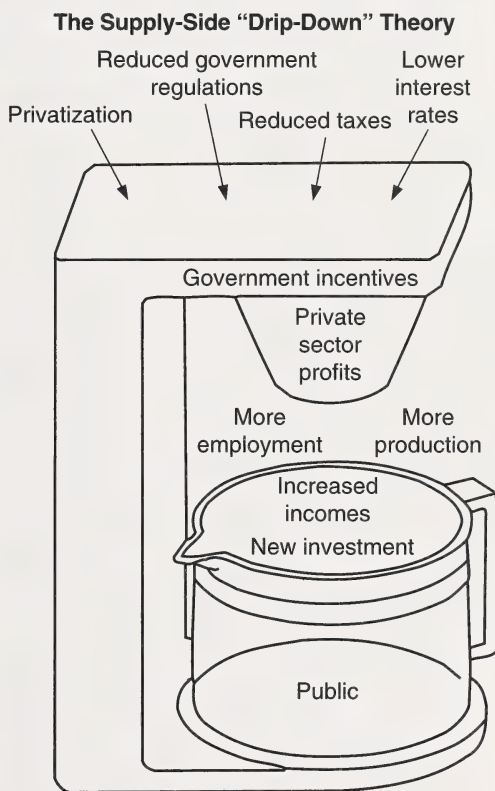
Keynesian or demand-side economics which had dominated economic thinking since the Great Depression of the 1930s emphasizes the amount of spending. By spending, consumers, businesses, and government create a demand for goods and services and this results in firms increasing production and producing more employment opportunities.

The economic theory that Reagan followed was previously known as supply-side economics which is a theory some proponents claim was first described by Adam Smith. Supply-siders emphasize the production side of the market. They feel that



rather than the government spending money to stimulate the economy, it should lower taxes (both business and personal), lower interest rates, and sell government-owned enterprises which would encourage business expansion. Reducing business taxes increases the profits businesses can make and thus encourages others to start businesses. Lower personal taxes gives people more to spend. Lower interest rates makes it easier for both businesses and individuals to borrow money and assists businesses that want to expand. Privatizing government companies removes unfair government competition and provides opportunities for private sector employment in these areas. This is also supposed to reduce the tax burden as it decreases government spending necessary to provide these services. Both Ronald Reagan and British Prime Minister Margaret Thatcher used this extensively.

When President Reagan took office, he was interested in tax reform, reasserting American global economic leadership, and subduing inflation. Reagan pointed out that the national debt was too high and he wanted tax cuts to stimulate the economy. The benefits of more people working and having more money to spend would trickle down to the less fortunate. He promised a balanced budget but instead added greatly to the nation's debt. Much of what he added to the debt came from his defense buildup. Although he deplored the budget deficits, he had to tolerate them in order to avoid tax increases and spending cuts. He did cut nonmilitary government spending but this saving was spent to pay the interest on the growing national debt. Some of the methods used to gain this spending cut involved downsizing the public service as he believed it should be smaller and more efficient. Privatization and deregulation were seen as positive ways to lessen government and to make the economy more competitive.



Supply-side theory states that if the private market is free to operate, then wealth will “trickle down” to the general public.<sup>1</sup>

<sup>1</sup> Diagram and caption taken from *Ideologies*. Reprinted by permission of McGraw-Hill Ryerson Limited.

President Reagan believed that accelerating inflation was destructive to the economy and wanted to control this. Federal Reserve chairperson Paul Volcker, a non-Reagan appointee, was allowed to drub inflation without pressure to relent before achieving the desired goal. Although Volcker was directly responsible for ending inflation, he could not have done this without Reagan's support. High interest rates were used to suppress inflation.

Reagan cut at the edges and altered the proportions of government functions but things remained much the same as prior to his taking office. While he had lowered the tax rates, the total tax bite for many Americans changed very little. He did end inflation and worked to bring about the shift from more government to less. Creating budget deficits to finance his defense spending left problems that the governments that follow have to deal with. As a result, the economic policies of President Reagan cannot be judged as an overall success or failure.

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### Clintonomics

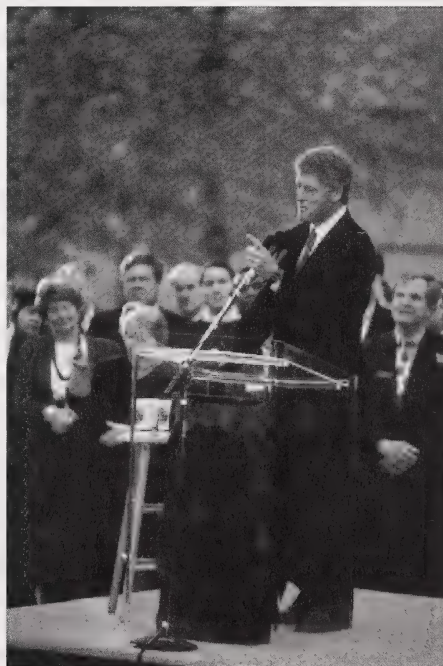
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*U.S. President Bill Clinton's economic plan  
is a juggling act in which he will try to cut spending,  
raise taxes, and keep voters happy all at the same time*

Bill Clinton, the latest new broom in the White House, is calling on Americans for sacrifice in a dramatic economic package now undergoing its baptism of fire in the U.S. Congress. Echoing President John F. Kennedy's famous "Ask not what your country can do for you" speech, he said, "The test of this plan cannot be what is in it for me? It has got to be what is in it for us?"

The economic package put together by the new president has three basic aims: to raise taxes, cut spending, and reduce the deficit. It didn't, however, start out in quite that way. In his election campaign, Mr. Clinton proposed a tax cut for the middle class and vowed to spend \$20 billion a year on roads and bridges and similar amounts for job training. But walking through the door of the White House has changed many a campaign promise, and the realities of a \$4 trillion national debt



and runaway annual deficits of more than \$300 billion have forced Mr. Clinton to hedge on his promises.

As Democrats (similar to Liberals in Canada), the Clinton team was expected to be a little left of centre, taxing the wealthy more heavily to pay for higher social spending. In reality, the Clinton economic plan seems more middle of the road or even conservative. Here are some of its main features:

- Income tax, as in Canada, is “progressive,” that is, the tax rate increases with higher incomes. The top rate of 31% would increase to 36% or more on annual incomes of more than \$200,000. A further surcharge of 10% would be made on incomes above \$1 million, bringing in an extra \$60 billion over four years.
- The tax rate on corporations would inch up from 34% to 36%, adding \$28 billion to federal revenue in four years.
- Elderly Americans with incomes of more than \$32,000 would be hit with an increase from 50% to 85% of the amount subject to taxation on Social Security benefits. Four-year federal gain: \$24 billion.
- A tax of 5% would be levied on all energy use. It would be called “BTU tax” (for British Thermal Unit). The tax would blow away the promise to reduce taxes on the middle class because it would hit all U.S. families with incomes over about \$30,000 a year. Gasoline, natural gas, home heating oil, and electricity would all be subject to the tax. Four-year value, \$60 billion.
- Other tax measures would limit tax deductions from executive salaries, enforce more tightly taxes on foreign companies operating in the U.S., and cut in half deductions for business meals and entertainment.

In all, Mr. Clinton’s tax-planning team estimates that these taxes would add more than \$190 billion to federal

revenues over the next four years. Most of the new taxes would click in January, but the controversial energy tax would be phased in gradually, starting in mid-1994.

On the other side of the accounts book are spending reductions.

- The defence budget would be cut by \$50 billion over the next four years, starting with a hefty \$8 billion reduction this year.
- Government administrative costs would be axed by \$3 billion. An additional \$6 billion would be saved by a cut of federal payrolls by 100,000 through not replacing people who quit or retire.
- The White House staff would be trimmed by 25%, and downsizing the limo fleet from 45 to 16 and other perks would save a token \$10 million annually.

To sweeten the bitter pill, President Clinton announced plans for new programs.

- The budget would include spending of about \$7 billion over the next two years on roads, bridges, and other infrastructure projects, far short of the amount promised in campaign speeches.

### Reaganomics

When President Ronald Reagan came to power in 1981 he said the U.S. national debt was too high. He pointed out in an early television broadcast that if the U.S. debt were shown as a stack of \$1,000 bills it would reach 119 kilometres into the sky. His prescription was tax cuts to stimulate the economy. The benefits of people having more money to spend would “trickle down” to the less fortunate. Did 12 years of Reaganomics (eight under Mr. Reagan and four under his successor George Bush) work? In his first telecast as president, Bill Clinton pointed out that the U.S. debt if shown as a stack of \$1,000 bills would now be 441 kilometres high.



- Though the cost is yet unknown, the president has pledged to allow students to repay loans through community work. A pilot project involving 1,000 students will start the plan off this summer, and it's expected that 100,000 or more will be taking part within four years. A national police corps and an apprentice job-training program are other Clinton ambitions. He calls all these "investments" for the future rather than spending. In total, Mr. Clinton has whittled down the \$120 billion in "stimulus spending" he promised as a candidate to about \$15 billion.

At first, Mr. Clinton's target was to make \$2 in spending cuts for every \$1 raised in higher taxes. His team of "deficit hawks" persuaded him to change that to \$3 in new taxes for every \$2 in spending cuts.

The White House number crunchers estimate that the plan will reduce the total of all deficits from 1994 through 1997 by \$325 billion. That, however, fails to take into account the Clinton

plans for a national health-care system which is now being looked at by task-force leader Hillary Clinton, the president's wife. There are 37 million Americans with no medicare insurance whatever, and higher taxes and far deeper spending cuts would be needed to finance full health care and still meet the goal of deficit reduction.

So far, polls show that Americans support Mr. Clinton's argument that the new tax burden will be spread so that nobody will be hurt too much. He will need continuing public approval as Clintonomics gets its acid test in Congress. Under the U.S. system of divided powers, his economic proposals are no more than that until Congress stamps its O.K. on them. He has the advantage that both houses have Democratic majorities more apt to favour a president of the same party. But special-interest groups representing seniors (higher Social Security taxes), the oil industry (the "BTU tax"), and many others will be out in force to fight various parts of the plan. Some say it may get through almost intact; others predict Congress will tear it to shreds.<sup>1</sup>



1. What were some of the economic ideas that were part of Reaganomics?

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<sup>1</sup> *Canada and the World* for the article "Clintonomics," by Charles A. White, May, 1993. Reprinted by permission of *Canada and the World*, Waterloo, Ontario.



2. Why did the United States national debt increase during Ronald Reagan’s terms as president?

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3. How do Clinton’s economic policies compare to Reagan’s?

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Check your answers by turning to the Appendix, Section 4: Activity 7.

Follow-up Activities

If you had difficulty understanding the concepts in the activities, it is recommended that you do the Extra Help. If you have a clear understanding of the concepts, it is recommended that you do the Enrichment.

### Extra Help

Match the following terms to the appropriate description.

- |                  |                  |                      |                 |
|------------------|------------------|----------------------|-----------------|
| a. New Deal      | f. mixed economy | k. stock crash       | p. expectation  |
| b. fiscal        | g. depression    | l. cost-push         | q. T.V.A.       |
| c. Boom and Bust | h. Keynes        | m. monetary          | r. recession    |
| d. poverty       | i. inflation     | n. alphabet agencies | s. Roosevelt    |
| e. demand-pull   | j. Hoover        | o. robber barons     | t. unemployment |

- \_\_\_\_\_ 1. a lack of money and possessions needed to supply life's basic needs
- \_\_\_\_\_ 2. J. P. Morgan and J. D. Rockefeller are these.
- \_\_\_\_\_ 3. 1929 Economic Crisis
- \_\_\_\_\_ 4. also known as the business cycle
- \_\_\_\_\_ 5. a temporary falling off of business activity
- \_\_\_\_\_ 6. the state of being without a job
- \_\_\_\_\_ 7. a long period of low business activity
- \_\_\_\_\_ 8. the president at the time of the Depression
- \_\_\_\_\_ 9. the president who brought in the New Deal
- \_\_\_\_\_ 10. the program to get the U.S.A. out of depression
- \_\_\_\_\_ 11. The T.V.A. and the C.C.C. are examples of these.
- \_\_\_\_\_ 12. Tennessee Valley Authority
- \_\_\_\_\_ 13. the economist John Maynard
- \_\_\_\_\_ 14. the policy of government spending and taxation
- \_\_\_\_\_ 15. the policy of controlling money supply in the economy
- \_\_\_\_\_ 16. Inflation: by thinking it will come, it will
- \_\_\_\_\_ 17. Inflation: high demand, low supply
- \_\_\_\_\_ 18. Inflation: costs of production on the rise

- \_\_\_\_\_ 19. an economic system that combines capitalism and socialism
- \_\_\_\_\_ 20. a time of generally rising prices

Check your answers by turning to the Appendix, Section 4: Extra Help.

Enrichment

You may do any one or all of the following Enrichment activities.

- 1. Using information from this section, complete the following chart.

Problems in the Economy	Explain How Keynesian Economics Works to Solve the Problems Listed
Poverty	
Inflation	
Unemployment	
Boom/Bust Cycle (Depression)	



2. If you have access to the video “Boom and Bust” from the BBC video series *Twentieth Century History*, please view it. The video outlines America’s path through the “roaring twenties” to the stock crash of 1929 and the Depression. Once you have finished viewing it, answer the following question.

Why did the economy of the United States go bust?

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3. If you have access to the video *Roosevelt and the New Deal*, view it at this time. The video gives an excellent account of Roosevelt’s actions during the Depression. It shows the increased role of government and the personal impact of Roosevelt as president. After viewing, answer the following questions.

- a. What actions did the government under Roosevelt take in order to lower the unemployment rate?

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- b. In what ways was the New Deal successful? Unsuccessful?

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- c. What qualities made Roosevelt such a popular president?

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Check your answers by turning to the Appendix, Section 4: Enrichment.



## Conclusion

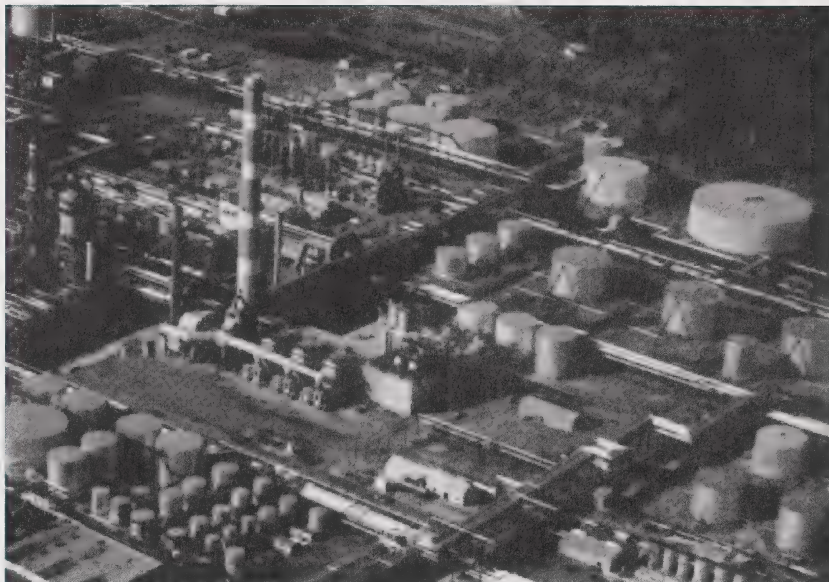
The New Deal and Keynesian Economics helped to show the need for economic systems to be adaptable. If an economic system such as capitalism was to remain in its traditional form it would soon become outdated and obsolete. The role of the government clearly took on greater importance after the implementation of the New Deal and the supporting theories of John Maynard Keynes. The mixed economy was beginning to take hold. When Ronald Reagan became president of the United States in the 1980s he began a movement away from Keynesian or demand-side economic theory towards supply-side economic theory that became known as “Reaganomics.”



### ASSIGNMENT

Turn to your Assignment Booklet and do the assignment for this section.

# Canada: A Mixed Economy



WESTFILE INC.

So far in this module you have been studying capitalism and the role governments play in such economic systems. When you think of an industrial plant, what role do you think the government should have in how it is operated or managed? Should the government set guidelines as to where such plants may be located? What about safety standards and pollution measures that such a plant should have to follow? Should there be a minimum wage and a set number of hours per week for the workers in the plant? If this plant is the largest employer for a nearby town and it runs into financial trouble, should the government assist its owners or let the plant close down? When you consider the impact of these questions and others, you should develop an understanding of why the government intervenes.

Canada is a country that has adapted pure capitalism to fit the needs of Canadian society. The Canadian economic system is a unique combination of capitalist and socialist policies.

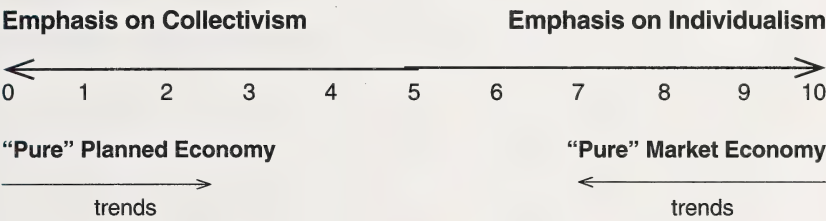
In this section you will learn about the eight roles of government in the Canadian economy. You will also learn why Canada is an example of a mixed economy.

Activity 1: What Is a Mixed Economy?

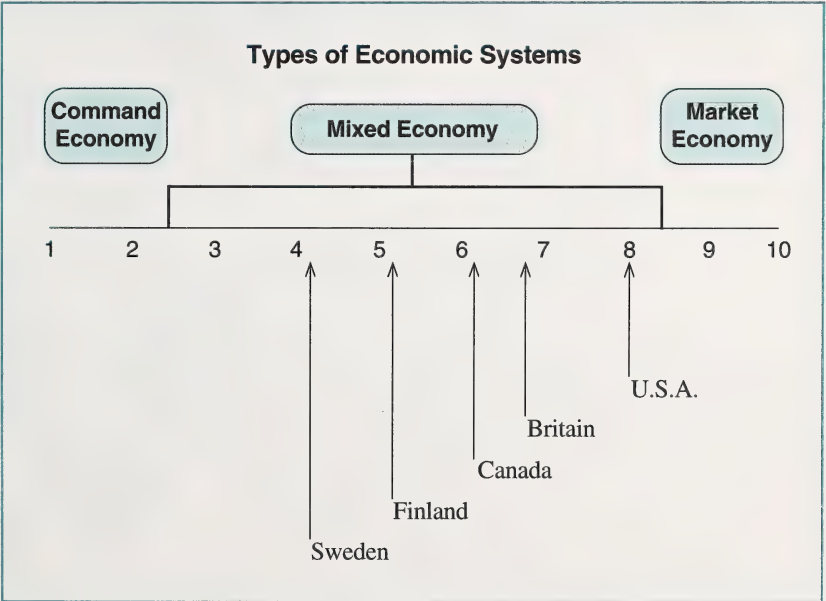
When in operation both pure market economies and pure planned economies experience problems. To correct these problems, the two systems borrow from each other.

Throughout the twentieth century governments in capitalist countries have become increasingly involved in their economic systems. This trend is often referred to as “creeping **socialism**.” On the other hand, capitalist practices are being introduced into Russia and other Eastern European countries that were formerly under communist rule. To help solve modern day economic problems, former Soviet planners are looking to Adam Smith rather than Karl Marx.

*Socialism: government ownership and/or control of the productive resources of a society*



A mixed economy is one which combines features of both market and planned systems. In most mixed economies, the majority of the nation’s resources are privately owned, but there is some government regulation. There is variation in the amount of government involvement in the economy. In some countries there is more government involvement than in others – but all are mixtures.





Canada is a mixed economy. The government takes an active role in certain areas of the economy. Under pure capitalism this would be unacceptable, but in a mixed economy it is the norm.

1. How would you define a mixed economy?

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2. Why do you think Canada follows the mixed economy model?

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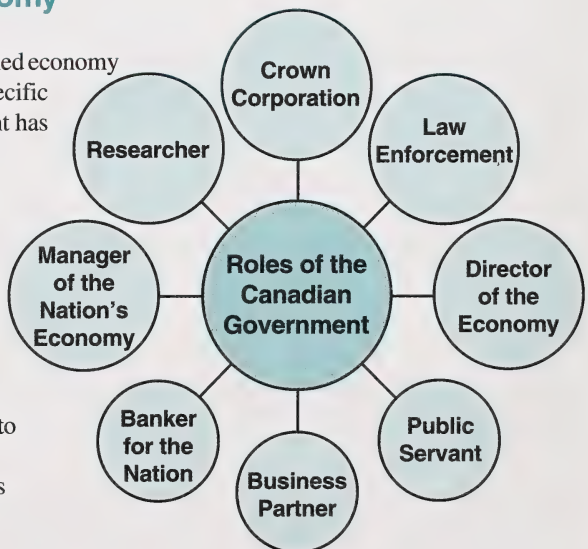
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Check your answers by turning to the Appendix, Section 5: Activity 1.

## Activity 2: The Roles of Government in the Canadian Economy

Within the Canadian mixed economy there are eight very specific roles that the government has assumed.

You will examine each one of these examples of government intervention in the Canadian economy. The Canadian government has adapted to meet the changing circumstances society has encountered.

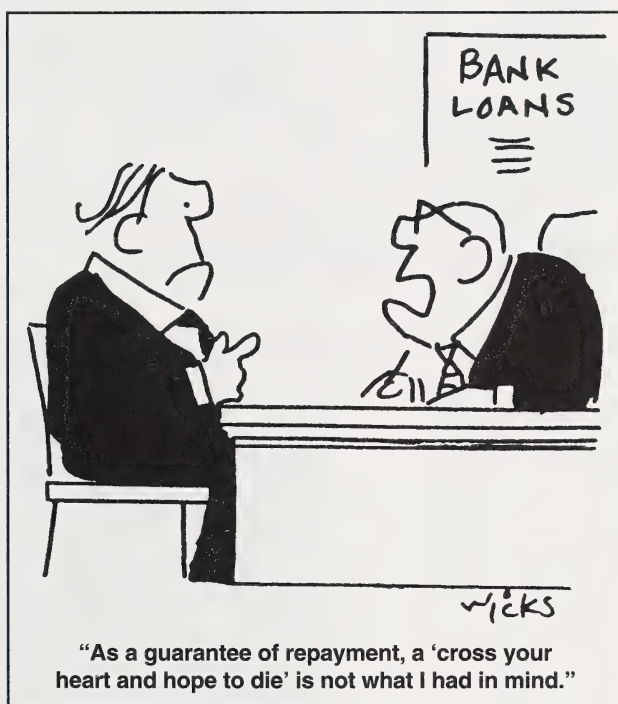




## Law Enforcement

In Section 2 you will remember that even under a pure capitalist system, the government had to ensure peaceful competition. The same holds true for a mixed economy. There must be rules and guidelines in an economy. If rules are broken, there must be someone there to punish the offender. There must be some sort of judicial system to decide what the punishment will be.

As an example to show how rules must be upheld, consider going to a bank to get a loan to buy a stereo. There are procedures and rules guaranteeing the loan, setting the rates of interest, and determining the time in which repayment must occur. You cannot simply walk into a bank, ask for money, and promise that you will pay it back.



If you cannot get a loan by following the rules, then you might decide to break the rules. If the man in the cartoon left the bank and came back with a gun and demanded the money, he would be arrested by the police and sentenced by a judge. The government clearly has an important role in setting and enforcing rules in the economy and society in general.

<sup>1</sup> Canadian Speakers' & Writers' Service Ltd. for the cartoon by Ben Wicks. Reprinted by permission of the Canadian Speakers' & Writers' Service Ltd.

1. Why is government involved in setting and enforcing rules in the economy?

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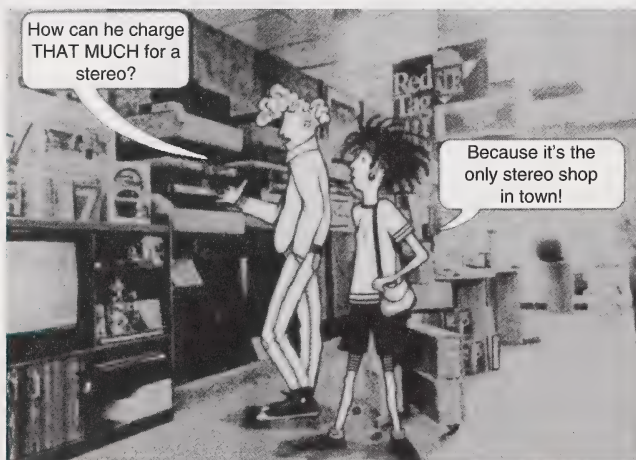
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Check your answers by turning to the Appendix, Section 5: Activity 2.

### Directing the Economy

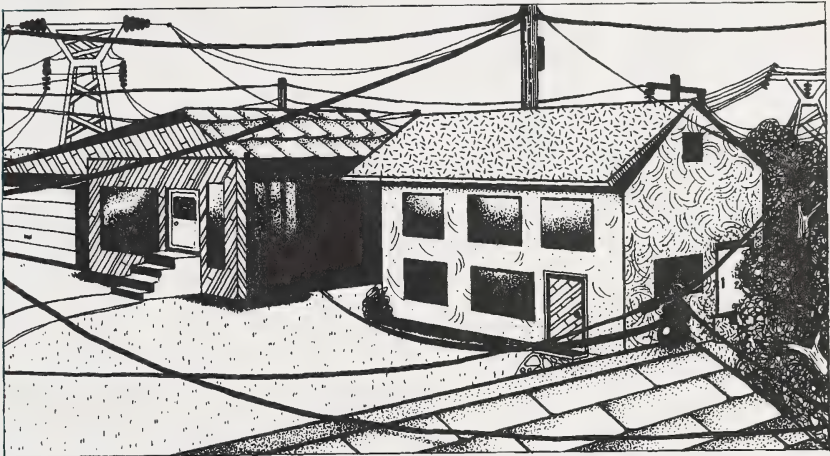
Another role which the Canadian government plays in the economy is to ensure that monopolies do not develop in the market. If government were to allow businesses to create a **monopoly** in any given industry, the consumer would face much higher prices. With no competition a business would have an unfair advantage. Therefore, the government watches and prevents monopolies in the economy.

***Monopoly:** a situation in which production is solely in the control of one company*



The Combines Investigation Act was passed in Canada in 1923. This act regulated monopolies, ensuring that the public interest was being guarded. If the government feels a monopoly is not in the public interest, it will take steps to break up the monopoly.

There are times though when the government does see a need for a monopoly to occur. Take, for example, certain service industries. It would be unrealistic to have many different electrical power supply companies. Something as important and complex as supplying electrical power to a city or region clearly must be controlled by government regulation. To allow many companies to supply electrical power could be very hazardous and confusing.



2. Why is it sometimes necessary for the government to allow a monopoly?

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Check your answers by turning to the Appendix, Section 5: Activity 2.

## Public Servant

Another role which the government plays in the Canadian mixed economy is that of a servant. Canada is concerned with the welfare of its citizens; therefore, the government's policies must reflect that. To ensure that many people are not starving on the street or without other basic needs, the government has programs to assist those in need. Programs such as old age security and welfare are examples of the government attempting to serve the needs of the less fortunate in Canadian society. This is certainly different than the view of pure capitalism, which would have emphasized "survival of the fittest."

*Social services: government programs designed to assist those in need*

*Universality: availability to all citizens of a society*

Another aspect of **social services** in Canada is **universality**. This means that the programs are available to all Canadians. The problem with this is that some people do not need government assistance. For example, an elderly couple with a high income will receive a monthly cheque from the government as part of the old age security pension program. However, if that couple's combined income is \$100 000, do they really need government assistance? This is an interesting question which requires further examination. Read the following article and cartoon; then answer the subsequent questions.

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### The Safety Net

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*Canada has set up an extensive system of social programs, but it's getting more and more difficult to finance it*

Some harsh words came out of the Department of Finance recently. The department released a 59-page booklet entitled *Canada's Economic Challenges* as part of the process of drawing up Finance Minister Paul Martin's first budget. The booklet outlines the state of the nation's social programs. And, what it sees it doesn't much like.

It dumps on the unemployment insurance program for being too costly and for encouraging people not to work. It says Canada spends more per capita on education than any other country among the Group of Seven industrialized nations, "But the results are less than spectacular." Other social programs are reviewed in uncomplimentary terms.

The process has begun of softening up the public for the harsh news it is going to get. Canada can no longer afford the wide social safety net we have come to rely on. The public purse, which pays for social programs, is empty.

A quarter of everything the government collects in taxes goes to pay the interest on the national debt, and the debt is continuing to rise at a dizzying speed.

How did we get into this mess?

For 60 years, Canadians were on their own. Government played almost no role in the daily lives of people. A small amount of money was handed out to the absolutely destitute but, generally, people were expected to look after themselves. Government help was restricted to emergencies – fires, floods, or severe injury to the family breadwinner. Help for the needy was felt to be work for the churches and other volunteer groups. Black Thursday changed everything.

On Thursday, 24 October 1929 the stock market collapsed. The value of company shares crashed and hundreds of thousands of people saw their life savings wiped out. The stock market crash ushered in the Depression and



### Reliance

On average, Canadians received \$20.40 in government transfer payments for every \$100 of earned income in 1990. According to Statistics Canada, the transfers include unemployment insurance, welfare, family allowance, pensions, and various tax credits. However, dependence on government cheques varies widely across the country. In Mount Carmel, Newfoundland, residents received \$68 from government for every \$100 in employment income. Meanwhile, the people of Yellowknife got just \$4 in transfer payments for every \$100 in employment income.

ushered out uncontrolled capitalism. The problems of the Great Depression were far greater than the existing system could cope with. With one in four Canadians out of work, governments began to realize they had to do something. What they did was sketch in the beginnings of the social welfare system.

The government responded with public works programs. Unemployed young men were sent to work relief camps where, for a small wage, they cleared trees and built roads and landing fields. A minimum wage, unemployment insurance, and a system that allowed farmers to apply for government credits were offered to Canadians. However, the prime minister of the day, R.B. Bennett, overstepped himself. The courts ruled, in 1935, that he didn't have the power to enact his social welfare plans. Another five years went by before the next prime minister, William Lyon Mackenzie-King enacted parts of Mr. Bennett's program.

All of what happened in the 1930s was a radical change from what had gone before. Completely new ideas developed such as the need for a more even distribution of the national income. Out of this came the notion that Ottawa should smooth out differences by

transferring money to the poorer provinces. Another new idea that developed was that Canadians should enjoy the same level of services no matter where they lived.

Along with the social legislation came a new view of economics. The government, it was now believed, should undertake high spending programs for the public good. In this way, the government could "prime the economic pump." Every dollar spent would have a "multiplier effect" – people with government cheques would spend their income in the private economy, and private industry would hire more workers to provide the goods and services in demand.

By the end of the 1930s, the Rowell-Sirois Royal Commission was studying Dominion-Provincial relations. From its findings came the start of more federal involvement in social welfare and health services. The Second World War stopped action in these fields for a while, though Unemployment Insurance was passed in 1940. In the post-war period, however, Ottawa's shadow was long in almost every social service area.

The Family Allowances Act came along in 1945. The Old Age Security Act of 1952 began the payment of pensions to all retired Canadians. In the same year, came the Blind Persons Act, and three years later the Disabled Persons Allowances Act. In 1965, a Canada Pension Plan was added, followed up by the Guaranteed Income Supplement in 1966. Two years later, Ottawa brought in a comprehensive health insurance plan.

But, we have been slow to recognize that our cradle-to-grave social welfare system has to be paid for. We haven't paid the full shot for these services and we've borrowed to make up the shortfall. There's a limit to how far you can go down that road, so Ottawa's next step was to increase taxes. This was done throughout the 1980s, but the deficit kept going up and people started to find

ways of dodging their taxes. In 1993, all levels of government spent \$94 billion transferring money to people, up from \$62 billion in 1989. This represents an increase of 50%, while the population went up by 5%, and the total value of goods and services by 9%.

Another, and growing, body of opinion says our debt problems can't be blamed on overspending on social programs. In 1991, a Statistics Canada study by economists Philip Cross and Hideo Mimoto fingered government tax breaks to corporations and the wealthy as the cause of our money woes. "It was not explosive growth in program spending that caused the increase in deficits in 1975," says the Statscan study, "but a drop in federal revenues relative to the growth of Gross Domestic Product and rising debt charges."

Whatever the cause of the problem, expenses have to be trimmed, and governments across the country have been forced to accept that tinkering with social programs won't work. What's needed is complete reform which translates, in most cases, into cutbacks of services.

One major principle behind our social programs was that all Canadians, regardless of need, should have access to them. This was called universality. The family allowance scheme was Canada's first universal social program; it provided a monthly payment to *all* child-rearing families in the country,

regardless of income. But, in the mid-1970s the government began nibbling away at family allowances.

By December 1992, the cost of the program had reached \$2 billion, and it was certainly no longer universal. In 1989, tax changes resulted in a "clawback" of baby bonus cheques from anyone making more than \$50,000 per year. This clawback tax allows the government to collect the allowance payments back from middle- and high-income families at tax time.\*

The cuts are now coming thick and fast:

- Last October, Alberta cut the basic monthly welfare rate to a single person from \$470 to \$394. In January it announced massive cuts to health and education.
- Earlier, Manitoba took a \$3 million bite out dental, optical, and pharmaceutical benefits for welfare recipients.
- Help for families in crisis is in shorter supply in Ontario because of government cutbacks in funding.

Given the financial condition of the country we can expect more of the same. And added to the list will likely be user fees for medical services, pension clawbacks, a redefinition of poverty to include fewer people, and massive reform of the unemployment insurance program.<sup>1</sup>

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**\* NOTE:** Effective January 1, 1993 Family Allowance was replaced by the Child Tax Benefit. The Child Tax Benefit which is tax free is based upon family income, the age and number of children in the family, and the marital status of the family's primary caregiver.

<sup>1</sup> *Canada and the World* for the article "The Safety Net," by Jane Sherwood, March, 1994. Reprinted by permission of *Canada and the World*, Waterloo, Ontario.

3. According to the article “The Safety Net,” what are two examples of social assistance programs?

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4. Explain what is meant by universality of government social assistance programs.

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Check your answers by turning to the Appendix, Section 5: Activity 2.

## Business Partner

The government is also quite often a partner in business. Because the government of Canada is concerned with the welfare of all Canadians, it must be interested in keeping companies in business.

To prevent business bankruptcies, which create unemployment, the government will take steps to assist businesses if they become financially troubled. Help from the government can come in the form of **tax write-offs**, or government **subsidies**. Often government assistance to business is enormous and, at some point, you might ask “How much is too much government intervention?” The following article examines the issue of the government as a business partner.

*Tax write-off: the deduction of business expenses from taxable income*

*Subsidy (grant): government economic assistance to a private company*

### Touching the public purse

Most business people call themselves capitalists. Capitalism is the system which lets them run their business with no interference from government. The business either makes a profit or it doesn't. If times are tough, or a service or product is no longer demanded by the consumer, then the company may fail. But the essence of capitalism, to these businessmen, is that they succeed or fail on their own initiative and skills.

On the other hand, recently we've seen a growing number of businessmen who, faced with a sticky spell, turn to the government for help. And there is a lot of help available in the form of subsidies, grants, tax write-offs, and “bail-out”

money. In effect, companies which make direct use of such schemes are putting the touch on the public's money through the government – money which the government has collected in the form of taxes. And once the government starts funding production facilities and services, capitalism as a system must surely suffer.

The government's involvement in business is staggering. In the year ended March 31, 1981, for example, the federal government took in \$8.13 billion in corporate income taxes; in the same year, it loaned or gave away about \$8 billion in the form of benefits to business.

Business grants and subsidies are

supposed to inject new investment capital into a company to enable it to stay alive. In turn, the company can then, theoretically, employ people, manufacture products for domestic use and export, and make enough money to pay back any grants and subsidies in the form of taxes.<sup>1</sup>



5. List and define the types of government assistance a business might receive.

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6. Why does the government sometimes become involved as an indirect business partner?

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Check your answers by turning to the Appendix, Section 5: Activity 2.

**Banker of the Nation**

One of the most important roles of the Canadian government in the economy is that of banker. The Bank of Canada is the national bank. The primary function of the national bank is to provide a sound monetary policy. (Refer back to Section 4 under the activity on Keynesian economics for the complete description of monetary policy.)

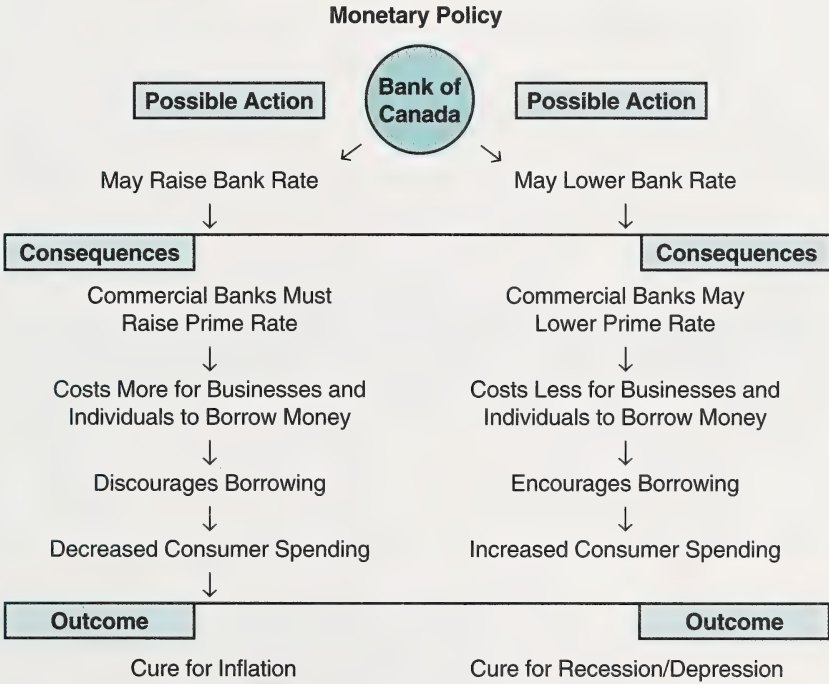
<sup>1</sup> *Canada and the World* for the article "Touching the public purse," by Jane Sherwood, November 1983. Reprinted by permission of *Canada and the World*, Waterloo, Ontario.



Generally, the Bank of Canada regulates the supply of money in the economy. When business activity is slow, the Bank of Canada attempts to make money easier to obtain. They do this by lowering the bank rate. The bank rate is the rate which the Bank of Canada charges commercial banks to borrow money. What the bank rate is will affect what the prime rate will be. The prime rate is the rate of interest that the commercial banks charge their best customers. The average consumer is charged a slightly higher rate of interest than the prime rate for the money borrowed.

Remember that if the interest rate is low, it encourages people to borrow causing spending and growth in the economy. The Bank of Canada can also raise interest rates which would decrease borrowing and spending. This is one way to control inflation.

The person in charge of the Bank of Canada is the Governor of the Bank who acts in consultation with the Minister of Finance. Together they direct the Bank’s monetary policy.



7. Name Canada’s national bank.

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8. What is meant by the term *bank rate*?

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9. What is meant by the term *prime rate*?

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10. Why does the Bank of Canada sometimes raise the bank rate?

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11. Why does the Bank of Canada sometimes lower the bank rate?

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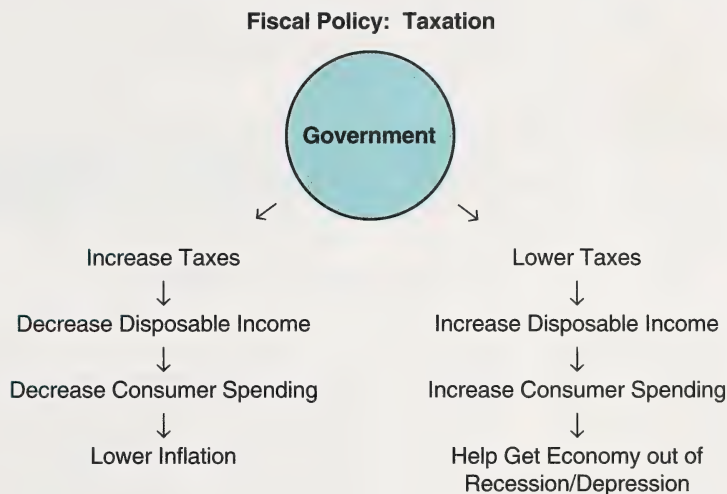
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Check your answers by turning to the Appendix, Section 5: Activity 2.

### Manager of the Nation's Economy

Another role of the government in the economy, like monetary policy, is drawn from Keynesian economics. By employing a sound fiscal policy, the government attempts to manage the economy. (For a description of fiscal policy refer to Section 4: Activity 5 of this module.)

To understand the fiscal policy regarding taxation examine the following diagram.



Remember from your earlier work that the government may spend its way out of a recession/depression. This is, once again, fiscal policy as well as monetary policy since the finance minister plays a role in setting bank rates. Government spending is also a part of the government's role as manager of the economy.

**Fiscal Policy: Spending**

GOVERNMENT ACTION	
Good Times	Bad Times
<ul style="list-style-type: none"> <li>• reduce government spending to avoid increasing inflation</li> <li>• tighten up social service payments (welfare) to slow consumer spending</li> </ul>	<ul style="list-style-type: none"> <li>• increase government spending in order to increase employment</li> <li>• increase social service payments (welfare) to increase consumer spending</li> </ul> <p><b>Note:</b> With these government actions comes a danger of developing a debt or deficit.</p>

12. Why would the Canadian government adopt a fiscal policy of lowering taxation?

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13. Explain what the fiscal policy regarding government spending should be in bad times.

Check your answers by turning to the Appendix, Section 5: Activity 2.

### Researcher for the Nation

A very odd yet essential role which the Canadian government plays in the Canadian mixed economy is that of researcher. Canadians want to know some very essential things and the government has assumed the role of finding the answers to questions. Statistics Canada is a government agency whose job it is to gather and make available to Canadians information on a wide variety of topics. The government itself may want information on changes in economic factors in order to properly manage the economy.

Other questions are answered by government agencies. A farmer wants to know the soil conditions in Saskatchewan. Or perhaps a business wants to know what the consumer price index is so that it can examine spending trends. Private industry may not want to supply these answers because it may not be profitable, so the government assumes the role of researcher for the nation.

14. What is Statistics Canada?

Check your answers by turning to the Appendix, Section 5: Activity 2.

### Crown Corporations

Lastly, the Canadian government takes on the role of providing those services which no one else wants to provide. Therefore, the government maintains a monopoly over certain industries such as national defence. What private company wants to become an army? Would it even be possible for a company to supply Canada with an army? Unlikely. So it becomes the job of the government.

Government businesses are called Crown corporations. A recent trend by government has led to some crown corporations being **privatized**, or sold to private industry. The following article discusses this trend.

*Privatized: when government-owned enterprises are sold to the private sector*



## The Business of Government

*Canada's geography dictates that sometimes governments have to take on businesses that private enterprise would not find profitable; sometimes governments go further*

Apparently governments, both federal and provincial, cannot resist the temptation of reinvesting in, and trying to run, businesses. Sometimes the results have been expensive and embarrassing mistakes. At other times, they have been able to make a go of it. But overall, the recent record has not been good.

Traditionally, governments have become involved in operating businesses to provide a vital public service that is too expensive or risky for private enterprise. These range from companies that provide electrical power, water, transportation services, communications, and other essential needs. Historical examples include: investing in the Canadian Pacific Railway, taking over the Canadian National Railway, starting Air Canada, and setting up the Canadian Broadcasting Corporation. All of these were seen as a means of linking the country together.

In other cases, such as electrical power utilities and municipal transit authorities, they operate as monopolies with no competition. But others, such as Air Canada and the CBC, function in the same way as other companies in the industry (see CROWN CORPORATIONS).

However, governments tend to get themselves into hot water when they stray too far from these usual types of businesses into other pursuits, such as

steel plants, cellular phone manufacturers, aircraft builders, sports stadiums, and oil companies. All too often, these misadventures result in red faces among politicians and lighter pockets for taxpayers.

Unlike business executives, politicians invest to meet social and political needs rather than simply to make money. They want to create or preserve jobs usually in areas where it will improve the local economy. They have not always assured themselves that the business has the markets etc., to survive on its own. Such enterprises run into problems because the people placed in charge of running these companies don't do so in a businesslike way.

It takes a certain toughness to run a business well. It means chasing customers aggressively and pushing suppliers for lower prices. When business is slow it means slashing the workforce. But, the reward for being tough and aggressive is taking home a share of increased profits. And, if that incentive is missing, there is less drive to succeed. At the same time, government-appointed board members sometimes lack the industry knowledge to help the executives survive in the business jungle.

A recent costly mistake is Novatel Communications Ltd. in Calgary. It was

### Quote...Unquote

International business strategist Kenichi Ohmae spoke recently about government help to business:

"Governments view industry almost entirely in terms of manufacturing. In the public mind, factories are where the jobs are. It doesn't matter that 75% of working people in (Canada) are now employed in the service sector. When political noses sniff the air, they always seem to do so just downwind of the nearest plant."

"When did you last hear of a government stepping in to rescue a services company – a software outfit, say? But let an old-fashioned steel company find itself on the ropes and it's time to call in the cavalry."

seen as a symbol for the new Alberta – a cellular phone manufacturer that would provide high-tech growth and jobs beyond the province's oil and gas wealth. It was founded in 1983 as a joint venture between the provincially-owned Alberta Government Telephones and energy giant Nova Corp.

It was a great concept. But turning it into a moneymaker was tougher than anyone expected.

The company turned sour. Management was only concerned about its own interests. The government-appointed board of directors provided no real help. As a result, spending got out of hand and products became increasingly out of step with what people wanted to buy. By 1989, problems had become so bad that its fate was sealed. According to a recent report by Alberta's Auditor General, the province's top financial watch dog, Novatel could wind up costing provincial taxpayers \$641 million.

The British Columbia Resources Investment Corp. (BCRIC) stuck to the tried and true – coal mining and oil – but it too has become a financial catastrophe. In their haste to assume greater control of British Columbia's vast mineral wealth, government leaders allowed

themselves to be out-negotiated by Edgar Kaiser, Jr. He sold his company, Kaiser Resources Ltd., to the B.C. government. In the process, he picked up a very lucrative consulting contract, as well as a low-interest \$18 million personal loan. The consulting contract had no termination clause so when BCRIC ended it a year later, Kaiser stopped paying back his loan. Eventually, the province had to write off \$10 million.

This was small potatoes compared to the hundred of millions of dollars lost from mishandling BCRIC's holdings in the North Sea off Scotland. Throughout the '80s, the company continued to write down the value of these assets. Not only did the corporation lose its shirt, so did many individual citizens. To make the purchase more politically acceptable in the late 1970s, the province gave every B.C. citizen five shares. Some people bought more, a few even invested their life savings in the company. Now, after more than a decade of continuing losses, these shares are all but worthless.

Sometimes, even success cannot save a government investment. In October, the Toronto Blue Jays became the first non-American baseball team to win the World Series. Millions of television viewers across North

### Crown Corporations

Crown corporations are wholly-owned federal or provincial organizations structured like private or independent enterprises. They carry out regulatory, advisory, administrative, financial or other services, as well as provide conventional goods and services. They enjoy greater freedom from political control than regular government departments. But ultimately they are responsible to Parliament through a minister of the Crown.

Some Crown corporations – CN Rail, Petro-Canada, and several provincial electrical utilities are among the largest businesses in Canada.

At the federal level, in transportation there is the St. Lawrence Seaway. In communications, we have the CBC. In finance, there is the Farm Credit Corporation. In addition, British Columbia, Saskatchewan, Manitoba, and Quebec offer automobile insurance through provincial Crown corporations.

In Saskatchewan since 1944, Crown corporations have been used to diversify the provincial economy away from agriculture. The same was true in Quebec after 1960, as the province invested heavily on power generating megaprojects to make manufacturing more attractive.

Currently, governments are pruning their garden of Crown corporations by privatizing or selling them off. One reason is to raise money; others are because they are too expensive to run, or the government believes it should not be in that business at all. For example, you can now buy shares in Petro-Canada and Air Canada although the federal government remains the biggest shareholder.

American and the world saw the Jays play in their home park, Toronto's SkyDome before full capacity crowds of more than 50,000 fans. But SkyDome, the \$580 million, state-of-the-art sports facility, the sole asset of its owner, Stadium Corp. of Ontario, an Ontario Crown corporation, is a financial basket case.

The province is now busy trying to unload the stadium to cut its losses. Cost over-runs added almost \$400 million to the original cost. And, the stadium's operating surplus will never be able to meet the annual interest payments due on its \$370 million mountain of debt.

The original estimated cost of the stadium was \$130 million. But, along the way, the developers added a hotel, a lavish fitness club, and other bells and whistles. Millions more were spent paying overtime to an army of workers slaving feverishly to finish the building on time. Throughout it all, the Ontario

government merely nodded its head in approval as the costs kept skyrocketing.

In a complicated deal, the province is ready to sell its share for \$100 million in cash plus debentures (a fancy name for IOU's) worth \$40 to \$50 million in today's dollars (over the life of the agreement, with interest it will be \$250 million). But the province considers it a good deal because if it did not sell now, it would be faced with annual interest payments of \$26 million most of which it would have to take from elsewhere to pay.

These are simply the biggest and most recent cases of bad government business deals. Other provinces have similar skeletons rattling around in their fiscal closets. Nova Scotia and its involvement in the Sydney steel plant, New Brunswick and its Bricklin auto plant, Newfoundland and its Come By Chance oil refinery, Quebec's investment in the Asbestos Corp., Saskatchewan's takeover of its potash industry, and Ottawa's bailout of Massey Ferguson which showed its thanks by moving its head office to Buffalo.

We have not seen the last of these mistakes. Somewhere out there is a company or industry that has to be saved by the public purse or a project that cannot proceed without government funds. Government leaders need to sit back and think long and hard about how these enterprises are to be financed, operated, and held accountable. By simply saying no to some of the proposals, they will save the taxpayers a lot of money and themselves a great deal of grief.<sup>1</sup>

### Seat Sale

A few years ago the government of Nova Scotia spotted what it thought was a sparkling business opportunity. A local company had developed a very special toilet seat. Built into it was an electric motor which reeled out sanitary plastic seat covers each time the toilet was used. The Nova Scotia government bought 200 of these seats at \$250 each, but they were never installed. Last July, the seats were sold at an auction in Milton, Ontario for \$1.50 each, bringing a total of \$300 to the hard-pressed treasury in Nova Scotia. But, it cost \$398 to ship the seats to the Ontario auction, and the auctioneer's fee was \$60.

<sup>1</sup> *Canada and the World* for the article "The Business of Government," by Ken Mark, February, 1993. Reprinted by permission of *Canada and the World*, Waterloo, Ontario.



15. What is a Crown corporation?

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16. Why does the Canadian government feel there is a need for privatizations?

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Check your answers by turning to the Appendix, Section 5: Activity 1.

## Follow-up Activities

If you had difficulty understanding the concepts in the activities, it is recommended that you do the Extra Help. If you have a clear understanding of the concepts, it is recommended that you do the Enrichment.

### Extra Help

In a true market economy the government would not have as much involvement in business as the Canadian government has. In a true planned economy there would need to be even more government regulation of business and less private ownership than exists in Canada. Since aspects of both market and planned economies are used in Canada's economic system, it is classified as a mixed economy.

Throughout Section 5 you examined the various ways the Canadian government regulates and is involved in the Canadian economy. It is this intervention in the economy that makes Canada's economy a mixed economy.

Review the notes in Section 5 dealing with the eight roles of the Canadian government in Canada's mixed economy:

- law enforcement
- director of the economy
- public servant
- business partner
- banker for the nation
- manager of the nation's economy
- researcher
- crown corporations

Use the material in Section 5 to complete the retrieval chart that follows.



The 8 Roles	Purpose of Government Intervention	Example
Crown Corporations	Some Crown corporations perform jobs that private industry will not do or cannot do.	CBC radio
Law Enforcement		
Director of the Economy		
Public Servant		
Business Partner		
Banker of the Nation		
Manager of the Economy		
Researcher		

Check your answers by turning to the Appendix, Section 5: Extra Help.

### Enrichment

Use your local newspaper to complete this activity. Find an article which shows the government in one of its roles for each of the eight roles of government in the Canadian economy. Record your findings on the following retrieval chart.

The 8 Roles	Name of Article	Evidence	Source
<b>Crown Corporations</b>			
<b>Law Enforcement</b>			
<b>Director of the Economy</b>			
<b>Public Servant</b>			
<b>Business Partner</b>			
<b>Banker of the Nation</b>			
<b>Manager of the Economy</b>			
<b>Researcher</b>			

Check your answers by turning to the Appendix, Section 5: Enrichment.

*Bilateral: involving two countries*

*Neo: new*

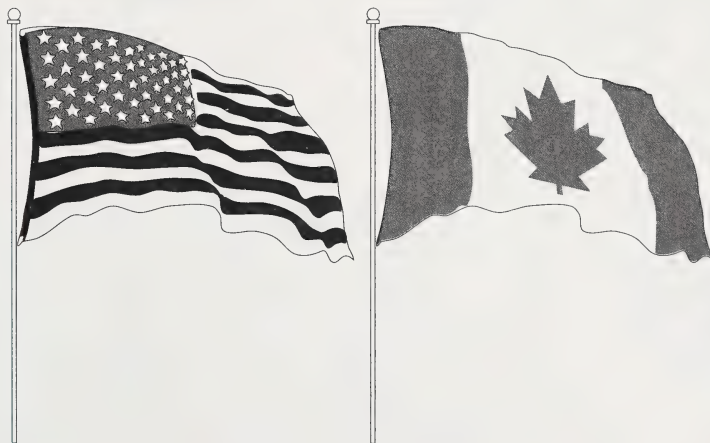
## Conclusion

The path that the Canadian government has embarked upon is an interesting one. In an age of supposed global cooperation, Canada has entered into an economic agreement which is **bilateral**. This is, of course, the free trade agreement with the United States.

The free trade agreement uses a mutually agreed upon schedule to lower trade barriers between the two countries. This may be a “free” trade pact between Canada and the United States, but it is making access into the North American market for other countries difficult.

Canada and the United States are attempting to create wealth for themselves. The idea of a nation or leader that attempts to create wealth at the expense of other nations was known as mercantilism. Perhaps what Canada is embarking on for the future is a form of **neo**-mercantilism. The free trade agreement is an example of bilateral economic agreement which attempts to distribute wealth on a regional level. It is difficult to predict where free trade will take Canada economically. The government may have to once again adapt to face a new economic challenge.

This challenge will be both practical and ideological. It will be practical in the sense that both the Canadian and American economic systems may be forced to change. Ideologically there is a challenge because traditional attitudes and beliefs may be brought into question. However, both Canada and the United States do share somewhat similar ideologies, so a positive outcome is likely.



## ASSIGNMENT

There is no assignment for this section.

## MODULE SUMMARY

Economic systems reflect ideas about human nature. The development of capitalism clearly displayed a belief that people are by nature competitive and self-interested. Through the search for profit, individuals in a capitalist economic system drive the economy.

You have also examined how economic systems are organized to deal with the production and distribution of goods and services in society. All systems must resolve the economic problem of scarcity, and the three economic questions must be answered. The way in which a country solves these concerns will determine its economic system. Under capitalism, individuals acting in a free market with supply and demand are left to respond to these important questions and concerns.

Pure capitalism—in its original form—was problematic and was required to adapt. This adaptation led to the mixed economy. Under this economic system the government assumed greater control in the economy.

Clearly, economic systems must continue to adapt and change to meet the changing environment and needs of society.


Assignment  
Booklet

### FINAL MODULE ASSIGNMENT

Turn to your Assignment Booklet and do the final assignment for this module.



# Appendix

	<b>Glossary</b>
	<b>Activities</b>
	<b>Extra Help</b>
	<b>Enrichment</b>

## Glossary

<b>Benchmark</b>	<ul style="list-style-type: none"><li>• a point of reference for comparison</li></ul>
<b>Bilateral</b>	<ul style="list-style-type: none"><li>• involving two countries</li></ul>
<b>Capital goods</b>	<ul style="list-style-type: none"><li>• machinery, tools, factories, and anything else used in the production of goods</li></ul>
<b>Capitalism</b>	<ul style="list-style-type: none"><li>• an economic system characterized by private or corporate ownership of capital goods Prices, production, and distribution of goods are determined in a free, competitive market.</li></ul>
<b>Centralization</b>	<ul style="list-style-type: none"><li>• concentrating power or authority in the hands of a central organization</li></ul>
<b>Consumer sovereignty</b>	<ul style="list-style-type: none"><li>• a system under which consumers have the freedom to purchase whatever goods they desire as long as they are produced and they can pay for them</li></ul>
<b>Contract</b>	<ul style="list-style-type: none"><li>• an arrangement to protect individual interests in an exchange of goods and services</li></ul>
<b>Crown corporation</b>	<ul style="list-style-type: none"><li>• business or industry owned by the Crown or its representative, the government</li></ul>
<b>Disposable income</b>	<ul style="list-style-type: none"><li>• money left over after taxes have been paid</li></ul>
<b>Distribution</b>	<ul style="list-style-type: none"><li>• the division of goods and services among several or many</li></ul>
<b>Economic competition</b>	<ul style="list-style-type: none"><li>• a system involving a large number of producers and buyers interacting in a free market</li></ul>
<b>Economics</b>	<ul style="list-style-type: none"><li>• the science that attempts to solve the problem of scarcity and satisfy people's wants</li></ul>
<b>Entrepreneur</b>	<ul style="list-style-type: none"><li>• a person who manages and assumes the risks of a business</li></ul>
<b>Equilibrium point</b>	<ul style="list-style-type: none"><li>• the point at which the quantity of goods for sale at a certain price is equal to demand for those good</li></ul>
<b>Exploitation</b>	<ul style="list-style-type: none"><li>• the making of unethical use of someone or a group of people for personal gain or profit</li></ul>
<b>Fiscal policy</b>	<ul style="list-style-type: none"><li>• a policy dealing with government spending and taxation</li></ul>

<b>GNP</b>	<ul style="list-style-type: none"><li>• gross national product, the total value of all goods and services produced in a country in one year It is hoped a steady moderate increase will occur in a given year.</li></ul>
<b>Goods</b>	<ul style="list-style-type: none"><li>• items that are used in production or sold to consumers</li></ul>
<b>Individual incentive</b>	<ul style="list-style-type: none"><li>• the motivation for an individual to act in their self-interest in the market</li></ul>
<b>Inflation</b>	<ul style="list-style-type: none"><li>• a time of generally rising prices This will cause a decline in the purchasing power of the dollar.</li></ul>
<b>Intervention</b>	<ul style="list-style-type: none"><li>• government involvement in the economy with the intent to change, modify, or direct</li></ul>
<b>Invisible hand</b>	<ul style="list-style-type: none"><li>• the economic theory that states that all society benefits indirectly through the actions of individuals or companies seeking profit</li></ul>
<b>Keynes, John Maynard</b>	<ul style="list-style-type: none"><li>• an economist who promoted government intervention in the economy He suggested increased spending and decreased taxation during recession and the opposite during periods of inflation.</li></ul>
<b>Market</b>	<ul style="list-style-type: none"><li>• a set of arrangements for bringing buyers and sellers together</li></ul>
<b>Means (modes) of production</b>	<ul style="list-style-type: none"><li>• the methods by which things are made in industry or agriculture</li></ul>
<b>Monetary policy</b>	<ul style="list-style-type: none"><li>• a policy having to do with the amount of money in circulation in the economy</li></ul>
<b>Money</b>	<ul style="list-style-type: none"><li>• an agreed-upon medium of exchange in the market</li></ul>
<b>Monopoly</b>	<ul style="list-style-type: none"><li>• a situation in which production is solely in the control of one company</li></ul>
<b>Needs</b>	<ul style="list-style-type: none"><li>• the desires for things which are essential for survival</li></ul>
<b>Neo</b>	<ul style="list-style-type: none"><li>• new</li></ul>
<b>Opportunity cost</b>	<ul style="list-style-type: none"><li>• the cost of making an investment that is the difference between the return on one investment and the return on an alternative investment</li></ul>
<b>Poverty</b>	<ul style="list-style-type: none"><li>• a lack of money and possessions needed to supply life's basic needs</li></ul>
<b>Private enterprise</b>	<ul style="list-style-type: none"><li>• an economic system based upon the values of private property and individual freedom</li></ul>
<b>Private property</b>	<ul style="list-style-type: none"><li>• a good or service belonging to an individual or company</li></ul>

<b>Privatized</b>	<ul style="list-style-type: none"><li>• when government-owned enterprises are sold to the private sector</li></ul>
<b>Productivity</b>	<ul style="list-style-type: none"><li>• the amount of goods or services produced in relation to the cost of production</li></ul>
<b>Recession</b>	<ul style="list-style-type: none"><li>• a temporary falling off or slowing of business activity</li></ul>
<b>Scarcity</b>	<ul style="list-style-type: none"><li>• an economic condition (problem) caused by unlimited wants and needs in the light of limited resources</li></ul>
<b>Services</b>	<ul style="list-style-type: none"><li>• activities performed to earn wages</li></ul>
<b>Social services</b>	<ul style="list-style-type: none"><li>• government programs designed to assist those in need</li></ul>
<b>Subsidy</b>	<ul style="list-style-type: none"><li>• government economic assistance to a private company</li></ul>
<b>Tax write-off</b>	<ul style="list-style-type: none"><li>• the deduction of business expenses from taxable income</li></ul>
<b>The three economic questions</b>	<ul style="list-style-type: none"><li>• What to produce? How to produce? Who gets what share of the production?</li></ul>
<b>Tradition</b>	<ul style="list-style-type: none"><li>• a belief or practice that has been handed down from previous generations</li></ul>
<b>Unit cost</b>	<ul style="list-style-type: none"><li>• the cost of producing one item or product</li></ul>
<b>Universality</b>	<ul style="list-style-type: none"><li>• availability to all citizens of a society</li></ul>
<b>Wants</b>	<ul style="list-style-type: none"><li>• the desires for things which are not essential</li></ul>

## Suggested Answers

### Section 1: Activity 1

1. They are land, labour, and capital.
2. Scarcity is defined as unlimited wants and needs in the face of limited resources.
3. What should be produced? How should it be produced? Who gets what share of the production?
4. There are unlimited wants and needs but only limited resources.
5. Capitalism is an economic system that stresses individualism, whereas socialism stresses group welfare. Capitalism promotes initiative, profit, self-interest, competition, and incentive. Socialism promotes collective action, group security, cooperation, and equality.



## Section 1: Activity 2

1. Answers will vary. Some possible answers are provided.

Goods	Services
refrigerator	haircut
guitar	insurance
hot dog	sales
car	firefighting
bike	teaching
stereo	legal services
table	banking
chair	medical assistance/advice
clothes	automotive repair
house	vacation/travel planning
television	nursing

2. A market is a set of arrangements for bringing buyers and sellers together.
3. a. Goods are produced or services are performed.  
 b. Buyers and sellers exchange goods and services for money.  
 c. The goods and services are used by the buyer.
4. The buyer and seller agree on a means to purchase the goods and services. Once the form of “money” has been agreed upon, the price of the good or service is decided and then exchange occurs.

## Section 1: Follow-up Activities

### Extra Help

1.   f   an economic system associated with profit, competition, and incentive  
  e   the basic economic problem  
  d   land, labour, and capital  
  c   science that attempts to solve the problem of scarcity  
  a   an economic system that uses parts of both capitalism and socialism  
  b   an economic system associated with cooperation, equality, and group welfare

- |            |          |
|------------|----------|
| 2. a. true | f. false |
| b. true    | g. false |
| c. false   | h. true  |
| d. false   | i. true  |
| e. true    | j. false |

### Enrichment

Answers will vary.

### Section 2: Activity 1

1. On a positive side, some countries and individuals achieved great wealth. The negative qualities include unfair competition and monopolies.
2. The monarch would grant a licence to a single company or individual.
3. Many people were shut out of the market because they were not granted a licence to operate.

### Section 2: Activity 2

1. Self-interest will cause producers to produce what is demanded by society because they are seeking profit.
2. Yes, the right to own private property is essential. If you do not own goods or services you cannot sell them. Therefore, without private property there could not be an exchange of goods and services for money.
3. Competition implies that there are two or more people or companies competing. Unless you allow individuals the freedom to pursue their self-interest, you will not have true competition.
4. If you were fortunate to be granted a licence to operate in a mercantile economic system, it would be profitable. However, if you did not get a licence you would probably fail. Capitalism, though, allows for greater individual freedom to compete economically, so it is an appealing economic system to many.

### Section 2: Activity 3

Your picture might show a variety of elements. The central one is competition and conflict. This means that there are (few) winners and (many) losers in general. The winners are thought to succeed because they are superior and the others are defeated as a result of their inferior qualities. The basic contest may be shown in terms of either a friendly competition such as a boat race or a bitter fight among armed groups. Some theme from nature, perhaps of predatory animals, might convey the idea also.

## Section 2: Activity 4

If you feel human beings are by nature competitive, you will believe that capitalism does reflect human nature. If you think human beings are by nature cooperative, then you might believe that capitalism does not reflect human nature.

## Section 2: Activity 5

1. The invisible hand is an economic theory that is meant to explain how society benefits through the indirect actions of individuals pursuing their own interests.
2. As producers and sellers search for profit, they indirectly benefit society. This is because through their search for profit they must supply what the consumer demands. If they do not they will not sell anything and they will go out of business. Through the course of production there will also be jobs for people, creating a happy, satisfied society – in theory.

## Section 2: Follow-up Activities

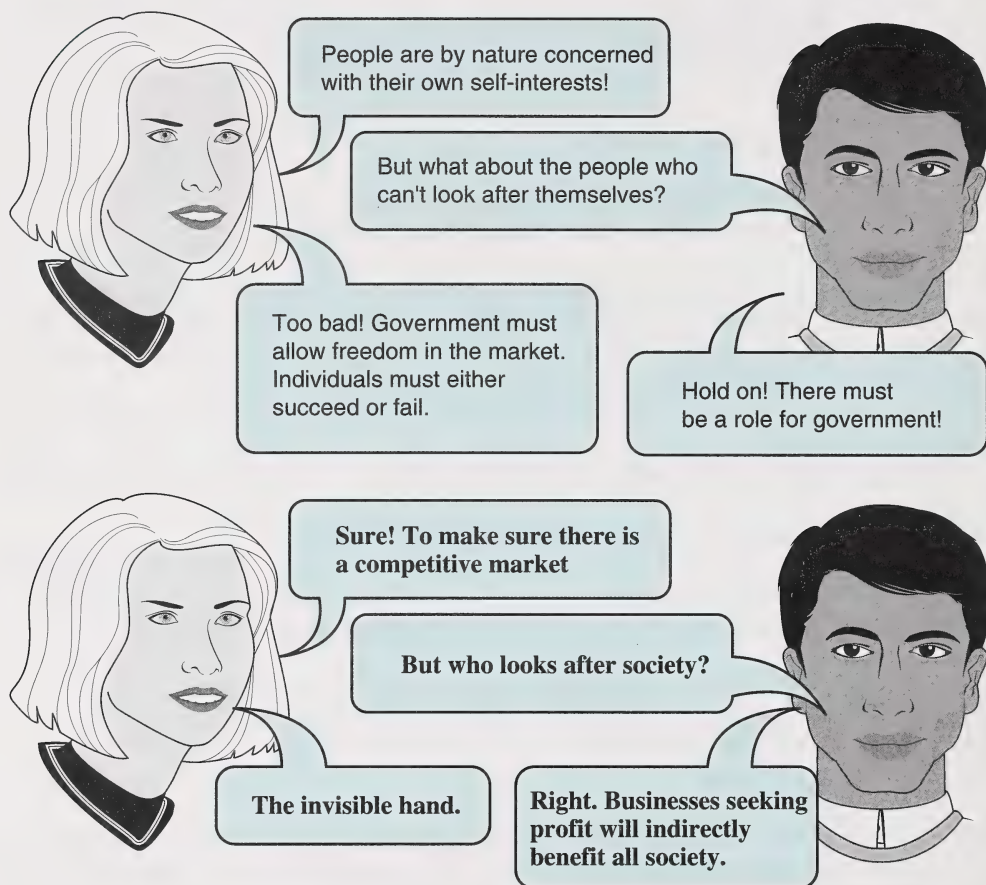
### Extra Help

1. Concept map A best represents mercantilism. Mercantilism was characteristic of little economic freedom, government restriction, and government intervention.
2. Concept map B best represents capitalism. The concept map deals with economic freedom, competition, individualism, and government non-intervention.

### Enrichment

1. In a capitalist economic system the government's job is to ensure a peaceful and competitive market. A greater role for government would go against the beliefs of capitalism. In capitalism there is a great deal of importance placed on the individual, who is left to either succeed or fail in the search for profit. Capitalism needs individuals competing in a market in order to deal with the production and distribution of goods and services in a society.

2. You could have completed the dialogue in a number of ways. Compare your version to the following.



3. a. Each term describes a major component of capitalism. Free enterprise – freedom of the individual. Market system – the role of the market in capitalism.
- b. Laissez-faire means “leave it alone.” This relates to the capitalist view that the government should not intervene in the economy.

### Section 3: Activity 1

The market exists so that buyers and sellers can have a set of arrangements so that exchange can occur. The market allows buyers and sellers to come together under understood guidelines. Without a market, there would not be efficient exchange between buyers and sellers.



### Section 3: Activity 2

1. Specialization means to become highly skilled in whatever job or service you choose.
2. By devoting more time to your chosen job or skill, you become better at it. As you get better, you produce more in relation to the costs of production. This is a result of the division of labour.
3. A doctor's skill is highly valued by society so he or she receives a high wage. The doctor may then use this money to purchase more in the market. The job of a bus driver requires less skill and training than does a doctor so the wage is lower. It is also more difficult to supply the demand for doctors because of the training needed.

### Section 3: Activity 3

1. Competition means to compete with another person or business to determine a winner.
2. Private property is a good or service belonging to an individual or company.
3. Individual incentive is the motivation for an individual to act in self-interest in the market.

### Section 3: Activity 4

1. The price of stereos when ten are sold is \$1500. This would mean that consumers generally find the price too high as only ten people are willing to buy at \$1500.
2. The price which corresponds to the highest demand for stereos is \$300.
3. Law of Demand: When the price of a product goes up, **fewer** stereos will be sold. When the price of a product goes down, **more** stereos will be produced.
4. The costs of production of a good or a service will include the profit taken at each stage of production. Also, there are additional costs added to the price of the good such as transportation costs.
5. There are many possibilities. Your drawing could be of a buyer refusing to pay the price that a seller wants for a product because it is too expensive or the quality is too low, or perhaps your drawing could show several people trying to outbid each other because they all have a strong desire to have the product or service.
6. The equilibrium price is approximately \$1200.
7. The quantity produced at the equilibrium point is approximately sixteen.
8. The demand will be approximately three stereos.

9. The demand will be ten stereos at \$900.
10. No, the producer of stereos will not supply the demand of fifty stereos at \$300 because there would not be enough of a profit at that price.
11. Individuals through their demand (desire) for goods and services can influence what will and will not be produced.
12. Those goods demanded by society will be produced. They will then be distributed to those with the funds.
13. If the goose lays golden eggs, this will increase the supply of gold without there being a corresponding increase in demand. This will have the effect of lowering the price of gold.

### Section 3: Activity 5

1. This is decided by the desire or demand for a good or service. If consumers decide that they are willing to buy stereos at a price which is profitable to the producer, then the producer will supply them.
2. In a capitalist system, goods and services are generally produced with the most effective and efficient use of resources. This is done to achieve a lower cost of production which will result in a higher profit for the producer.
3. Goods and services are produced, quite simply, for those who can afford to purchase them.
4. It is the alternative choice not taken. If you are thinking of buying a bike or a stereo, and you buy the stereo, the bike is the opportunity cost.

### Section 3: Activity 6

You may simply say that private enterprise allows for a great deal of individual freedom. It is also an economic system that efficiently deals with the distribution of goods and services in society by allowing supply and demand to influence production and distribution.

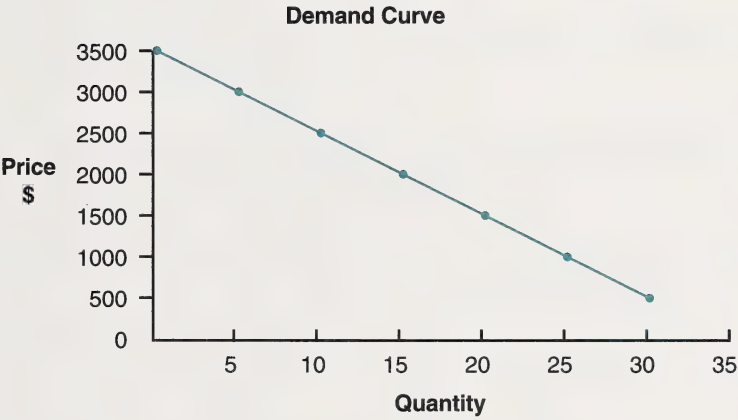
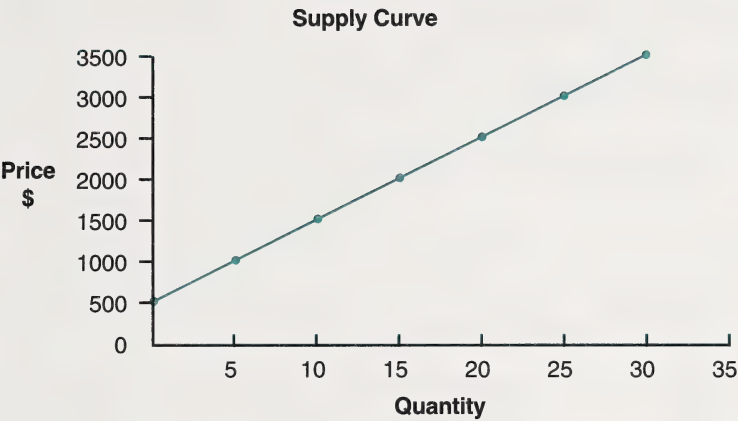
### Section 3: Follow-up Activities

#### Extra Help

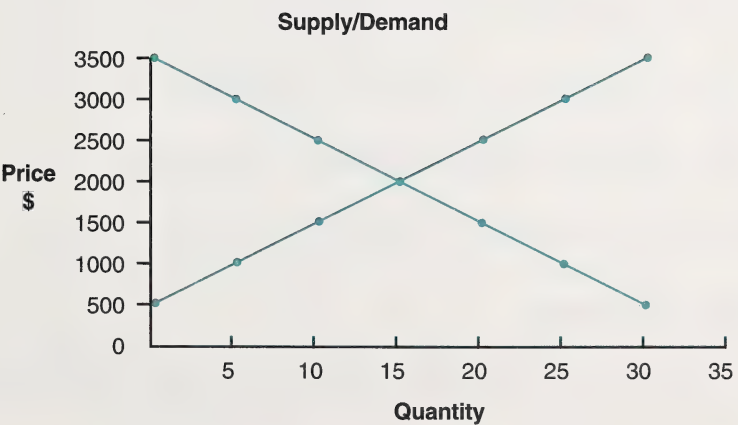
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|------|------|------|------|-------|
| 1. e | 3. i | 5. j | 7. h | 9. f  |
| 2. d | 4. b | 6. c | 8. g | 10. a |

Enrichment

1.



2.



3. The price is \$2000.
4. The quantity supplied is 15.

### Section 4: Activity 1

1. The updated deficit for Alberta is 1.7 billion.
2. Men such as J. D. Rockefeller and J. P. Morgan were the robber barons.
3. People were upset because the robber barons had become so wealthy. It was thought that they were taking more than their fair share of the wealth.
4. Under pure capitalism there was supposed to be decentralized decision making. There was not supposed to be a monopoly of economic power which is what the robber barons had.
5. To a degree yes, capitalism encourages people to seek their self-interest and profit. Therefore, you will see some very wealthy people in a capitalist economic system.

### Section 4: Activity 2

1. Poverty is a lack of money and possessions needed to supply life's basic needs..
2. Many people began to see poverty not as a sign of weakness but rather as a result of circumstances. The crash made many wealthy people poor.

### Section 4: Activity 3

1. An economic boom is a period characterized by full employment, high inflation, high investment, and high demand. It is a time of economic growth and expansion.
2. An economic bust is a period characterized by high unemployment, low inflation, low investment, and low demand. It is a time of economic decline.
3. The percentage of unemployed at the start of the depression was 3.2%.
4. It took three years for the unemployment rate to reach 23.6%.

### Section 4: Activity 4

1. Overextension of credit is borrowing far more than you can actually afford to. This, of course, is a problem if whoever lent you the money wants it back in a hurry.



2. If people are unemployed, then they do not have money to direct towards consumer spending. If people are not spending, then businesses may go out of business which will cause even more unemployment. Thus, it is a problem that can continue to grow unless action is taken to stop it.
3. Answers will vary, but here are some suggested research questions:
  - When was the New Deal introduced?
  - Why was the New Deal introduced?
  - Where was the New Deal used?
4. The answers will vary here, but should be based on what you've learned in the activity.
5. Roosevelt was using government intervention to correct problems in the economy. This intervention would never occur under pure capitalism.
6. The government used the alphabet agencies to put people to work. This encouraged consumer spending which was to increase employment.
7. It would seem from the graph that there was some success. From 1933 to 1937 there was a large decrease in the unemployment rate.
8. You might say that this was because Roosevelt seemed to be taking an active role in solving economic problems. He provided strong leadership.

#### Section 4: Activity 5

1. In economically difficult times, such as depression, Keynes felt the government should step in.
2. Keynes felt that strong government spending would get the economy going again.
3. Both wanted government spending in the form of capital work projects. Both the New Deal and Keynesian economics proposed that these projects would lower unemployment, increase consumer spending, and cause economic growth.
4. Inflation is a time of generally rising prices.
5. When people expect inflation, they tend to contribute to it. "Spend your money now because it won't be worth anything tomorrow."
6. When there is a very high demand for a product with a low supply, the supplier can raise the price of a good or service because so many people have the desire to buy.
7. In good times prices generally go up due to increased demand for goods. This causes workers to request higher wages which in turn causes producers to raise the price of their good or service. This is due to the increased cost of production.

### Section 4: Activity 6

1. Keynes is charged with changing capitalism, creating a “mixed-up economy.”
2. Free enterprise is the best way to protect people (invisible hand). There should be no government intervention.
3. First, he said that times were much simpler when Smith had written his ideas. Second, he said monopolies had gained too much power.
4. A country’s government must assume control of long-term planning for its economy.
5. A mixed economy is one which uses characteristics of both capitalism and socialism.
6. You may take either side, but ensure that you have properly justified your position.

### Section 4: Activity 7

1. President Reagan wanted to control inflation, bring in tax reform, and bring down the national debt to stimulate the economy. He wanted to see less government. He thought if more people were working they would have more money to spend and that this would have a trickle-down effect so that the less fortunate would also benefit.
2. Under Reagan’s leadership there was a buildup of defense and military spending was increased. He did not want to raise taxes and/or make massive spending cuts to pay for the increase in defense so the national debt continued to grow.
3. President Clinton needs to raise taxes and cut spending in order to deal with the deficit that threatens the country’s economy. He will have to spread the tax burden even though he campaigned on cutting taxes for the middle class. He will need to downsize government in order to achieve spending cuts. He will have to make a serious attempt at reducing the deficit rather than just talking about wanting it reduced.

### Section 4: Follow-up Activities

#### Extra Help

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| 1. d | 6. t  | 11. n | 16. p |
| 2. o | 7. g  | 12. q | 17. e |
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| 4. c | 9. s  | 14. b | 19. f |
| 5. r | 10. a | 15. m | 20. i |

### Enrichment

1.

Problems in the Economy	Explain How Keynesian Economics Works to Solve the Problems Listed
<b>Poverty</b>	By using capital works projects, people will have jobs, so fewer people will be poor.
<b>Inflation</b>	Monetary and fiscal policy may be used to limit the amount of money and spending in the economy.
<b>Unemployment</b>	Once again, capital works projects will put people to work.
<b>Boom/Bust Cycle (Depression)</b>	The government must become involved in both good and bad times to correct the economy. By controlling the amount of money in an economy using fiscal and monetary policy, a government can either encourage a decline or growth in the economy. By changing government taxation and spending, a government can affect consumer spending, causing economy growth or decline.

2. You must mention points such as these:
- There was an overextension of credit.
  - There was no investment into the economy.
  - There was very little confidence in the economy.
  - Consumer spending decreased.
  - Due to low demand and spending, factories closed down and people lost their jobs.
3. a. It used capital works projects to employ people which caused an increase in consumer spending. This, it was hoped, would cause growth in the economy.
- b. The New Deal appeared to lower unemployment. It also increased confidence in the United States economy. However, it did not totally remove the United States from economic hard times.
- c. Roosevelt displayed leadership, strength, compassion, and understanding. The American people felt that they could trust him. This ability to instill trust made Roosevelt one of the most popular American presidents.

### Section 5: Activity 1

- Answers will vary. A mixed economy is one that combines features of both a planned economy and a market economy. It will have a mixture of public and private enterprise.
- Answers will vary. The Canadian government has adapted to meet the changing circumstances society has encountered. People have certain demands and expectations of the Canadian government.

## Section 5: Activity 2

1. Government is involved in setting and enforcing economic rules so that a peaceful, competitive market is achieved.
2. It is sometimes necessary for the government to allow monopolies because some services such as electrical power and telephone systems are very complex and important. They must be operated by a single company with government regulation to ensure society receives the best available service.
3. Old Age Security Pensions and the former Family Allowance (now Child Tax Credit) are examples of social programs.
4. Universality means that the social programs are available to all Canadians regardless of need.
5. One type of government assistance is a tax write-off which allows a business or an individual the opportunity to deduct business expenses from taxable income. Another type is government financial assistance to a private company.
6. The government will sometimes assist business in order to help businesses to stay alive. The company can then employ people and manufacture products. The government then hopes to get back the money that it put in by taxing the company and its employees.
7. The Bank of Canada is Canada's national bank.
8. Bank rate is the interest rate the Bank of Canada charges the commercial banks to borrow money.
9. Prime rate is the interest rate that the commercial banks charge their best customers to borrow money. The average consumer is charged slightly more than the prime rate.
10. The Bank of Canada will do this to discourage borrowing, which will slow consumer spending. This will act as a check on inflation.
11. The Bank of Canada will lower interest rates in order to make money easier to borrow. This will encourage consumer spending. The effect of this would be to cause growth in the economy, hopefully curing a recession or depression.
12. The government would lower taxation to increase consumer spending causing economic growth.
13. In bad times the government should increase spending to ensure employment stays high. It should also increase social programs to ensure that those in need are helped.
14. Statistics Canada is one of many government agencies that supply services to Canadians. Statistics Canada provides information on a variety of topics which many Canadians find useful in their lives.



15. A Crown corporation is a government-owned business.
16. It is to allow Crown corporations to compete and expand. It also allows the government to recover part of the money it has invested in them through taxation. Besides raising money, there is a growing philosophy that government should not be in such businesses.

## Section 5: Follow-up Activities

### Extra Help

The 8 Roles	Purpose of Government Intervention	Example
<b>Crown Corporations</b>	Some Crown corporations perform jobs that private industry will not do or cannot do.	CBC radio
<b>Law Enforcement</b>	There must be rules and regulations to ensure a fair, competitive market. These rules must be enforced.	the police and the court system
<b>Director of the Economy</b>	This ensures that monopolies do not emerge unless they are wanted. Two examples are electrical power or telephone systems.	Combines Investigation Act
<b>Public Servant</b>	The government provides social services to ensure that those in need are taken care of.	unemployment insurance or welfare
<b>Business Partner</b>	The government becomes a business partner to ensure that businesses stay in business and keep people employed.	Canadair
<b>Banker of the Nation</b>	In this role the government regulates the amount of money in the economy. This allows the government to either indirectly increase or decrease consumer spending.	Bank of Canada can raise or lower interest rates.
<b>Manager of the Economy</b>	By adjusting government taxation and spending, the government can either slow down an economy or cause economic growth.	In bad times, a government can increase spending on capital works projects.
<b>Researcher</b>	This is done to provide necessary information to Canadians on a variety of topics.	Statistics Canada

### Enrichment

Answers will vary here depending upon the articles you chose to use.



## ***NOTES***

## **NOTES**



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## NOTES

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